91-1166

No. _____

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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1991

PHONETELE, INC.,

Petitioner,

vs.

THE AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INCORPORATED; BELL TELEPHONE LABORATORIES, INCORPORATED; PACIFIC TELEPHONE AND TELEGRAPH COMPANY,

Respondents.

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. In a Section 2 case, how must a finder of fact weigh the respective components of predatory intent versus innocent intent in consideration of a regulated monopolist's justification of its exclusionary conduct? Must innocent intent predominate in order for a defendant to prevail on the affirmative defense?

2. How long is it permissible for a trial court to delay in rendering a decision before the delay constitutes grounds for reversible error?

3. Has there been an impermissible appearance of impropriety which would require vacatur of the trial court's decision?

THE PARTIES

Petitioner-plaintiff, Phonetele, Inc., is a California corporation, previously involved in the design, manufacture, sale and service of a specialized type of telephone terminal equipment. Defendants consist of American Telephone and Telegraph Company, its affiliates Bell Laboratories and Western Electric Company, Pacific Telephone and Telegraph Company and the 7 "Baby Bell" regional companies formed as a result of divestiture ordered by the United States District Court.

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GLOSSARY OF TERMS

"Ancillary Equipment" - refers to telephone terminal equipment manufactured and sold almost exclusively by non-utility companies. Ancillary equipement generally enhanced an owner's telephone system but ancillary equipment did not replace tradtional telephone company equipment which is non-ancillary such as PBX, KTS, and other similar telephone terminal equipment.

"ATT" - means the American Telephone and Telegraph Company prior to divestiture in 1984. Sometimes, where appropriate, the terms "Bell" or "the Bell System" is used to mean ATT and its pre-divestiture Operating Companies throughout the United States as well as Western Electric Company and Bell Telephone Laboratories, Inc.

"CPE" - means "customer-provided equipment", non-utility telephone terminal equipment. Also, referred to at times in court or agency opinions as "COAM" for "customer-owned and maintained equipment".

"CPUC" - means "California Public Utilities Commission".

"FCC" - means "Federal Communications Commission".

"FRO" - means First Report and Order, 56 FCC2d 593 (1975), FCC registration program for ancillary terminal equipment.

"Interconnect company" - means a vendor of customer provided equipment.

GLOSSARY OF TERMS (continued)

"Phonetele I" - means the first Circuit Court opinion in this matter, 664 F2d 716 (9th Cir. 1981).

"Phonetele II" - means the second Circuit Court opinion in this matter, 889 F2d 224 (9th Cir. 1989), attached as Appendix A.

"SRO" - means Second Report and Order, 58 FCC2d 736 (1976), FCC registration program for non-ancillary terminal equipment.

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Respondents.

PETITION FOR A WRIT OF CERTIORARI

OPINIONS BELOW

The Ninth Circuit Court of Appeals filed its opinion in this case on November 6, 1989, a copy of which is attached as Appendix A [sometimes Phonetele II]. The appeal involved a District Court unpublished opinion entitled "Findings of Fact, Conclusions of Law, and Memorandum Opinion" filed by the District Court for the Central District of California on July 14, 1988, a copy of which is attached as Appendix B. On or about November 17, 1989, Phonetele filed its "Petition for Rehearing and Suggestion for Rehearing En Banc", ("Petition for Rehearing") a copy of which is attached as Appendix C. The Ninth Circuit filed its order denying Phonetele's Petition for Rehearing on October 17, 1991, a copy of which is

attached as Appendix D. Previously, in the first appeal in this action, the court reversed a finding of implied immunity in favor of ATT; the court also established Law of the Case. (sometimes Phonetele I).

JURISDICTIONAL STATEMENT

The Ninth Circuit filed its opinion on November 6, 1989, in Phonetele, Inc. v. ATT, No. 88-6353. Phonetele filed a timely Petition for Rehearing on November 17, 1989, which the Ninth Circuit denied by its order filed October 17, 1991. Phonetele filed this Petition for Writ of Certiorari within 90 days of that date. Jurisdiction of this Court is founded on 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

Sections 2 of the Sherman Act, and 15 of the Clayton Act, respectively, provide in pertinent part:

> Every person who shall monopolize ... any part of the trade or commerce among the several states ... shall be deemed guilty. ... (15 U.S.C. §2)

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States ... and shall recover threefold the damages by him sustained. ... (15 U.S.C. §15)

STATEMENT OF THE CASE

A. Preliminary Statement and Law of the Case

The real question posed is what did the finder of fact in the instant case take into account and how did the court weigh the evidence of predatory versus innocent intent in order to conclude that ATT proved its affirmative defense? After Phonetele I, if defendants had put on no substantial additional evidence at trial, Phonetele would have prevailed according

to the Law of the Case. What was the nature and quality of the evidence supporting a finding in ATT's favor? Did the purported "innocent" intent, which the District Court found, predominate over predatory intent in order to establish ATT's affirmative defense?

In the previous appeal of the implied immunity, Judge (now Justice) Kennedy, writing for the court in Phonetele I, established very specific, narrowly crafted tests to govern the further proceedings in this case. Expressly, the Court also rejected the notion, argued by ATT, that antitrust immunity would result merely because the FCC permitted the post-Carterfone connecting arrangement tariff, called FCC 263, to go into effect.

Among other things, Phonetele I recognized that ATT's so-called "foreign

attachment" tariffs employed PCAs as the exclusive means to install non-utility terminal equipment to the telephone network constituted unlawful, unnecessary restrictions in order to avoid technical damage to the network.[1] Utilities charged installation and monthly "service charges" for PCAs; a purchaser of CPE was forced to pay these charges in order to install CPE. In all cases, involving sale of CPE, the CPE supplier was required to contact his competitor, a Bell company or other utility, so that the installation of the CPE could be accomplished through a PCA. The connection of CPE to the telephone line, in this fashion, always had to be arranged through the utility competitor, a situation wholly unsatisfactory and unique in

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[1]Tariffs carry force of law. Carter v. ATT, 365 F2d 486, 496, (5th Cir. 1966).

the annals of business. PCAs engendered numerous other objections which go to the merits; they are not pertinent at this time.

In brief, the competitive situation at the time may be described as follows. Interconnect companies, such as Phonetele, designed and manufactured their equipment with essential safety features. Having necessarily absorbed the cost for network protection, they objected to PCAs as duplicative, costly and unnecessary. They sought direct connection through a simple terminal block. They fought PCA requirements at both the state regulatory Commissions and the FCC. At stake was an issue of fair competition: the right to connect CPE directly to the network without PCA design impediments, availability problems, and costs. Phonetele found itself unwit-

tingly thrust into the vortex of the national issue by virtue of its early litigation before the California PUC ("CPUC") which began in January, 1971.

After Phonetele I, it stood established that ATT would be liable for monopolization under Section 2, unless it proved its regulatory affirmative defense. The Court characterized the defense one of "factual necessities". (p. 738) The subsequent appeal, Phonetele II proceeded on the same premise: "The district court assumed throughout this case, and AT&T does not dispute, that AT&T's restrictions on interconnection would be an antitrust violation unless AT&T could justify the restrictions." (Appendix A, p. 6)

The specific affirmative regulatory defense set forth in Phonetele I, which governed the trial, states:

If a defendant can establish that, at the time the various anticompetitive acts alleged here were taken, it had a reasonable basis to conclude that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority, then its actions did not violate the antitrust laws. (664 F2d at 737-38; emphasis added).

Phonetele I further elaborated:

At this stage of the proceedings, it appears this inquiry will depend largely on whether the facts show the companies did reasonably conclude, given their expertise, that uncontrolled NCSU [Network Control Signalling Unit] interconnection would endanger their own equipment or disrupt their own signal transmissions in identifiable ways, and also that the tariff as filed was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such real harm from occurring. (p. 738, add bracket).

. . .

The defendants may not justify their actions based on some mistake of law in interpreting the FCA, or judicial or FCC decisions. It will not be open to a defendant to argue that it was entitled as a matter of right to file any tariff it chose or that it was obligated to file a tariff absent

> the kind of factual necessities we have outlined above. After the Carterfone decision, a defendant may not assert that it was entitled by law or agency policy to a monopoly in the furnishings and supply of terminal equipment. Id.

In other words, ATT could not take the position at trial that it was empowered to protect the national telephone network, if that position were at odds with communications policy articulated by the regulatory authorities. Indeed, the trial court, acknowledged the above test as its "marching orders". Yet, the trial court misapplied the Law of the Case by ignoring, among other things, that no regulatory authority recognized ATT's purported factual imperatives as "legitimate."

Notwithstanding the specific regulatory test carefully crafted in Phonetele I in 1981, the courts subsequently ignored

and/or misapplied the Law of the Case. They effectively conferred upon ATT an immunity without proof of the requisite "regulatory mandate" which the defense requires. The courts fundamentally disregarded the underlying regulatory decisions (a pure matter of law). The courts failed to consider and to weigh the respective components of (a) predatory intent versus (b) innocent intent, in order to determine which predominates in divining requisite general intent, necessary to satisfy Section 2.

One of the principal areas of confusion arose because the courts below accorded great significance to ATT's myriad "economic" arguments, matters wholly irrelevant and immaterial to the regulatory defense.

B. Ancillary Equipment Economic Issues Irrelevant

The District Court recognized that the Phonemaster, Phonetele's only product, involved "ancillary" equipment.[2] Concerns of technical harm to the network constituted ATT's only stated opposition to ancillary CPE. Yet, the District Court and Circuit Court's heavily relied upon "economic" arguments to justify ATT's conduct under Section 2. Because only "ancillary" equipment was considered by the District Court, however, potential

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[2]Ancillary equipment did not replace any traditional utility provided equipment such as PBXs, KTS, etc. Therefore, economic issues were completely irrelevant to ancillary equipment issues. The District Court, however, relied heavily upon economic issues argued by ATT to justify it conduct vis-a-vis Phonetele. (see Appendix B, pp. 76-82, beginning with the introductory sentence, "By approximately 1972, it became apparent that financial considerations needed to be considered. ...")

economic issues, associated with displacement of non-ancillary equipment were irrelevant.

The courts below failed to recognize that the FCC expressly refused to permit economic issues to interfere with enactment of a registration program to govern direct connection of CPE as an alternative to the PCA tariffs. On appeal, the Circuit Court compounded the trial court's error of mixing up economic issues as part of ATT's affirmative defense. For example, "Interconnection posed technical and economic problems of considerable complexity". (p. 6) This statement, included citation to FCC decisions which compel precisely the opposite conclusion. (see FRO and SRO). ATT understood that more liberalized interconnection necessarily meant competi-

tion. The attendant "economic" burdens from competition are universal to any company; they are not unique to regulated utilities. Moreover, the FCC has dictated that economic arguments are entirely irrelevant for purposes of ATT's affirmative defense.[3] The courts below thus departed fundamentally from the regulatory mandate.

Other evidence of the trial court's fundamental error permeates the decision. Examples include the following: (1) "...

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[3]In Phonetele I, the court was explicit in its reasoning that only "network harm" arguments were appropriate considerations of ATT's regulatory defense. Phonetele I cited the famous Carterfone decision, "... ATT could consider the safety of the telephone network in formulating the new tariff." 664 F2d at p. 725, n. 21. Nowhere does Phonetele I, which governs the Law of the Case, permit the regulatory justification on the basis of "economic harm" arguments and, indeed, such arguments properly can occupy no legitimate place in the regulatory defense.

[the FCC] acknowledged that the effect of such attachments or substitutions of equipment in the telephone system provided both technical and potential financial problems of wide range and effect." (Appendix B, p. 51; brackets added) (2) Bell contended then (and believes to this day) that the 'unbundling' of telephone charges inherent in a system which allows free substitution to the network will cause a significant rise in local revenue rates as a consequence of decreasing revenue from long distance service and provision of businesstype telephone equipment." (Appendix B, p. 79). (3) "... over the years, local regulatory agencies had placed pressure on the BOC's to shift as much of the overhead as feasible to business equipment, to the end that residential equipment would receive lower

rates. Rate structures accomplishing what the local regulatory agencies insisted on became imbedded in the Bell System as a whole. The result was, in general, that local residential telephone service was 'subsidized' by long distance service and business service." (p. 77).

These wideranging "economic" issues represent areas appropriate for primary jurisdiction which regulatory agencies in their expertise, not the courts, should properly address. However, the FCC and CPUC insisted upon addressing economic issues entirely separate and apart from registration. (see infra. at pp. 52-54). Both the trial court and Circuit Court committed reversible error by their critical reliance upon economic issues.

C. ATT's Position in a Nutshell

ATT stonewalled any type of certif-

ication to replace PCAs unless, and until, all the "economic" issues and technical issues (on design, testing, installation, and maintenance) were in place to its satisfaction. It refused to engage in any type of iterative or step-by-step approach urged by the CPUC and FCC, so that some emerging base of experience with direct connection could result. ATT's position was doctrinaire, unsupported by any evidence, and without sanction by any regulatory authority.

ATT's Federal Regulatory Department was responsible for working with the FCC. An ATT Federal Regulatory Department document dated November 8, 1971, titled, "A Credibility Gap Exists", admitted:

> The carriers find it necessary to argue the "polution" (sic) case, i. e., a little was all right, but the expansion will indeed cause serious impact on the network. This inability to demonstrate cases of harm, the

> "future" potential argument and the failure to produce logical arguments against specific situations (as opposed to the broad, general argument) is causing the manufacturers, interconnect companies, users and regulatory bodies to question the real nature of network harm and to challenge the expansive efforts which Bell insists must be taken to avoid the network pollution." (Ex. 5474, pp. 12, November 8, 1971).

Network pollution, coupled with no meaningful statistical data that CPE harmed the network (any more than utility equipment), provided thin gruel to support ATT's regulatory justification defense. Absent, irrelevant arguments, of an "economic" nature, ATT could not prevail. Economic harm arguments at best raised typical questions of the costs of competition, a universal concern for any regulated or non-regulated company. If anything, ATT's sensitivity to its vulnerability from competition supports predatory intent; it is irrelevant as a justification.

C. Cases in Conflict with Phonetele II and the trial court

The decision in the instant case conflicts with the decision in Litton Systems, Inc. v. ATT, 700 F2d 785 (2d Cir. 1983). The underlying facts and regulatory background in Phonetele and Litton are virtually identical. Litton affirmed a substantial antitrust award against ATT. In large part, Litton relied upon findings that regulatory imperatives predominate, and these imperatives inexorably led Litton to a finding of "predatory", not innocent, intent. Litton's treatment of identical regulatory authority was proper and requires similar treatment in the case at bar. Litton found that the regulatory authority had rejected ATT's purported "factual imperatives" under which ATT attempted to justify its conduct. If the

courts below had interpreted the identical regulatory authority consistently with Litton, the findings perforce had to result in ATT's liability. A second case from the Fourth Circuit, North Carolina Util. Comm'n v. FCC, 552 F2d 1072 (4th Cir. 1977), cert denied, 434 U.S. 874 (1977) has previously determined that the so-called economic issues are irrelevant to ATT's justification of its PCA tariffs (e.g. opposition to certification, "... the other side of the interface tariff coin"). [see Litton 700 F2d at 809] Yet, the courts in the case at bar have ignored, if not undermined, the North Carolina case.

D. Phonetele, the Phonemaster and brief Regulatory Background; ATT's inability to Compete; Baseless and Repetitive Claims

Phonetele's predecessor partnership, began business in 1969 and Phonetele, Inc. was incorporated in 1970 in the State of California. Since January, 1971, when Phonetele's product was first ready for market, Phonetele has been embroiled in litigation of one type or another with the Bell System. None of the litigation has been of Phonetele's choosing. Rather, Phonetele was forced to file Complaints before the CPUC just to stay in business. The utility required hardware was duplicative of protective circuitry contained within the Phonemaster, Phonetele's only product. Among other problems caused by PCAs, the non-availability and charges for

the PCAs acted as a severe marketing deterrent to sales of the Phonemaster. Such litigation alone would render it impossible for almost any company to survive. Even so, Phonetele remained actively in business, some years profitable, until 1988.

The Phonemaster is a programmable computer, custom programmed to control telephone usage in accordance with the owner's wishes at a particular location or locations. The Phonemaster is a compact, stand-alone toll and message unit restrictor or "controller". Beginning with its initial conception and design, the Phonemaster contained internal protective circuitry (an "interface" card), which accommodated the Phonemaster's direct electrical connection to the network. The Phonemaster's sole purpose is prevention

of unnecessary telephone charges by compelling efficient use of the owner's telephone system.[4]

Because the Phonemaster, unique at the time, necessarily decreased ATT's revenues, there existed additional competitive reasons to drive Phonetele out of business and to prevent expanded use of the Phonemaster.[5] (see United States v.

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[4]The Phonemaster represented a product years ahead of its time in that it addressed telephone usage problems. Only in the mid 1970s did such products, to reduce telephone usage charges, become a standard telephone equipment feature. Also, the Phonemaster was constructed in a state-of-the-art modular architecture which utilized micro-computer technology just beginning to find its way into telephone equipment. Almost invariably, independent companies such as Phonetele, not the utilities, introduced such state-of-the-art technology to telephony.

[5]Several exhibits cite ATT's recognition that the "controller" market represented a "vast market", however, Bell policy was to offer such equipment on a "demand basis only".

ATT, 524 F. Supp. 1336, 1352, n. 64 (D.C. 1981), hereinafter sometimes "government's case".

Phonetele's attacks on the PCA tariffs unwittingly propelled it onto a direct collision course with ATT's policy to require PCAs in all cases. The collision course had nothing to do with the issue whether the Phonemaster or CPE harmed, or was likely to harm, the telephone network in any fashion. In Phonetele's case, the Bell System massed a formidable engineering and management "task force" in order to thwart Phonetele in regulatory hearings as well as in the marketplace.

On January 10, 1972, during the pendency of the hearings in Phonetele v. PTT, a Complaint case before the CPUC, PTT's Chief witness against Phonetele

admitted to his fellow task force members:

> ... we are not able to demonstrate that ... the Phonemaster ... [causes] actual harm to our facilities, services, personnel or customers, although our engineers have done an excellent job of analyzing the potential for harm inherent in connecting these devices to the network by direct electrical means. (Ex. 5117, at p. PS1B1910).

On February 14, 1972, just before the continued hearings before the CPUC, Don Erickson, Chief of ATT Engineering Group responsible to enforce PCA tariffs, sent a letter to Mr. Schiavoni, Head of ATT Engineering. It documents a conference call among the Bell System task force members working on the Phonetele Complaint case. The letter reveals the national implications incident to a probable CPUC rebuff of Bell System's insistence that the ZZAGM (a PCA for the Phonemaster) be required. ATT feared such a rebuff would result in a "direct connect" order for the

Phonemaster. In part, the letter read:

> ... they [Bell System people working on the case] were concerned that if they insisted upon the use of their connecting arrangement (ZZAGM -- see attached), the Commission would rule that protective connecting arrangements were unnecessary. This would mean direct electrical connection and create waves that would wash on the shores of every other Commission, including the FCC. (Ex. 5129; emphasis added)

In 1968, a Landmark case called Carterfone opened up the terminal equipment market to competition. After hearings which were widely followed throughout the industry, the FCC struck down ATT's tariff as "unreasonable and unduly discriminatory." Carterfone, 13 FCC2d 420, 423 (1968). The FCC noted, "[n]o one entity need provide all interconnection equipment for our telephone system any more than a single source is needed to supply the parts for a space probe." (at p. 424). It was clear that Carterfone,

while not directly involving direct electrical connection of the Carterfone device, applied equally to direct electrical connection.

After Carterfone, ATT filed its "connecting arrangement" tariff, designated "FCC 263". FCC 263 became effective January 2, 1969, and thereafter all utilities, including the Bell Operating Companies filed conforming tariffs in every state jurisdiction. FCC 263 went effective without any investigation or ruling on its lawfulness. The FCC admonished ATT at the time that the tariff was its own, not the FCC's. [In the Matter of ATT Tariff Revisions, 15 FCC2d 605, 610 (1968)]. Like its predecessor tariff which Carterfone struck down, the post-Carterfone tariff, FCC 263, also failed to distinguish between equipment which was

"harmful" or "harmless" to the network. Rather, the tariff was premised on an unstated, improper, assumption that all CPE was harmful to the telephone network, despite the fact that no showing of harmfulness had been made. (see Phonetele I at p. 724 and note 38, recognizing that failure to distinguish between equipment which is harmful or harmless to the network gave rise to the tariff's illegality).

From Carterfone forward, the ultimate outcome became increasingly more certain: the PCA tariffs prescribing PCAs as the exclusive means to connect CPE were unlawfully restrictive and discriminatory. The FCC, like the California Supreme Court in Phonetele v. PUC, 11 Cal.3d 125, 113 Cal. Rptr. 16 (1974), merely permitted the tariffs to remain in place until a suit-

able alternative program of engineering standards, then under consideration, had been enacted. The regulatory authorities expressly disapproved of the Bell position stonewalling certification and chastised Bell for failing to cooperate in establishing standards to interconnect CPE.[6]

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[6]On page A-14 of its opinion, the Circuit Court in Phonetele II acknowledged, "... Phonetele's position ultimately prevailed both before the FCC and before the CPUC ... ." Elsewhere however, the Circuit Court's "sleight of hand" exonerated ATT: "AT&T was specifically permitted by the regulatory agencies to require a PCA to be used with the Phonemaster during a period when those agencies had not yet resolved the dispute between the merits of certification and protective devices. Until this issue was actually decided against PCAs, AT&T acted reasonably in requiring a PCA." (emphasis added) Such a statement is nothing short of incredible because a regulator's mere "permitting" the PCA to remain in effect does not, under any authority, constitute a regulator's recognition or endorsement of the PCA as "legitimate". Phonetele I in fact rejected this very notion. (664 F2d at 733). Litton also promptly disposed of the identical argument, "... the FCC's failure to strike down a tariff at

A senior executive from ATT's Federal Regulatory Department wrote in November, 1972, that Phonetele's was a "precedent setting case on certification" and the coordinated Bell System effort would "try to minimize" Phonetele's effect on "our other FCC-oriented programs". (Ex. 5181).

Therefore, it is well documented in the record that in early 1972, Bell admitted that (1) it opposed direct connection of the Phonemaster because "it was a precedent setting case on certification" which "... would mean direct electrical connection and create waves that would wash on the shores of every other Commission, including the FCC." and (2) that standards could have been developed for

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the time of its filing does not make the conduct lawful, particularly where, as in this case, the agency specifically declines to rule on a tariff's legality." (at p. 808).

the direct connection of the Phonemaster "if asked to do so".[7] Moreover, all during this time, the evidence shows that ATT could have proposed standards for direct connection for all types of CPE within a few month's time in 1967-68. (Ex. 5418; 5410, 5412).

After Phonetele v. PUC, in April, 1974, all major regulatory issues had been decided in favor of Phonetele. At the time of Phonetele v. PUC, the parties informed the Supreme Court that a CPUC

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[7]Don Black, PTT's engineer who headed up the PTT team against Phonetele, admitted at trial that there was no engineering reason in December, 1970, that the Phonemaster could not have been certified for direct connection. (RT 800:20-25; 801:1). Conceding this, and given the proof that ATT possessed no empirical data to support its argument that CPE harmed the network, how can one explain why the court in this case permitted ATT to monopolize the terminal equipment market, including Phonetele's entry into it, for over 9 years with impunity?

General Order had been issued to promulgate a certification program. For this reason, and in deference to agency expertise, the Supreme Court merely permitted the utility-provided PCAs to remain in place (status quo). Mere permission that a tariff remain in effect lacks sufficient "coercion" to play any part in supporting ATT's affirmative defense. (Phonetele I, 664 F2d at 733).

E. ATT's Weak Competitive Position

In 1972, ATT commissioned McKinsey and Company to prepare a Report on the Bell System's ability to meet interconnection competition. In its Report dated January 23, 1973, McKinsey arrived at three major conclusions: (1) Bell is suffering from major handicaps in sales effectiveness; (2) underlying cause of problems is lack of explicit business

strategy and supporting product/market strategies for terminal equipment; [and] (3) To correct these problems, management must commit itself to comprehensive action program. (Ex. 5550, p. PD3A1522, numbers and brackets added).

Given such reality, it is no small wonder that ATT was convinced of its inability to compete fairly at the time.

F. Opinion in Phonetele II

In Phonetele II, the Ninth Circuit conducted a cursory recital of the regulatory background and then blessed the District Court's finding that ATT acted reasonably at the time of the events. At the same time, paradoxically, the Circuit Court recognized, the "issue was actually decided against PCAs ... ." Appendix A, p. 14. The Circuit Court commented that several of the trial court's findings

were "not clearly erroneous", notwithstanding the fact that on every one of these points the contemporaneous admissions from ATT's own documents in the record leads to an opposite conclusion.[8]

Phonetele II also stated that Phonetele was not prejudiced by the procedure of permitting written testimony, even though 4 years elapsed from submission to decision. This is wrong; Phonetele was

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[8]At oral argument, the Ninth Circuit Panel suggested that Phonetele might file annotations of the evidence supporting its position, since Phonetele claimed that the trial court's findings were pervasively incorrect, almost without exception. On or about September 15, 1989, after oral argument on August 11, 1989, Phonetele filed 88 pages of "Annotations on Behalf of Phonetele, Inc." in response to the Panel's suggestion. Apparently, the Ninth Circuit Court did not read the Annotations. If it had, it would be clear that the trial court Judge gravely distorted the evidence to make findings which contradicted the contemporaneous ATT documents in the record.

prejudiced. The "prejudice" lies in the fact that the trial court's memory invariably favored ATT's written direct testimony, even though numerous contemporaneous "admissions" via documents on several major points, forced an opposite finding. (see infra., at pp. 54-58).

Lastly, the Ninth Circuit said the it was aware of "no case holding that a district court commits reversible error by taking too long to decide a case." (p. A-18).[9]

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[9]Phonetele also knows of no such case. However, there should be law on such an important issue. The case at bar presents this Court with a prime opportunity to address the issue of undue judicial delay and what consequences, if any, when the delay is unconscionably long as here. This issue is both timely and important to the fair administration of justice. It represents an issue which is intimately involved with modern-day cases and dockets. Phonetele adds that it has not been responsible for the undue delays at both the trial court and appellate court levels.

REASONS FOR GRANTING THE WRIT

The instant Petition presents two questions of first impression: First, how must the court weigh the nature and quality of a defendant's "intent" in mixed motivation monopolization cases? How should the courts properly analyze/weigh the intent when both predatory and innocent intent components are present? When mixed motives are present, must legitimate motives predominate or is it sufficient if they exist in any part, no matter how substantial? May a court recognize as "legitimate" in regulated monopoly cases those proffered factual imperatives which the regulatory authority, exercising primary jurisdiction, has already rejected? Second, how long is too long for a trial court to delay its decision before reversible error occurs? A corollary, in

such cases of delay: how much prejudice must a complaining party demonstrate before reversible error occurs?[10] Inherent in consideration of the above questions is the proper relationship between the antitrust courts and the regulators which previously decided the issues under

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[10]In the case at bar, Phonetele can demonstrate that the District Court's findings of fact are pervasively flawed. The Annotations, which Phonetele filed in the Court of Appeals, well support Phonetele's contentions on this point. On the most pivotal factual points of the case, in repeated instances, the District Court erred. One of the better examples is the trial court's finding that the Phonemaster "... did not include in its circuitry ... protective electronics." (Appendix B, p. 108). ATT never even suggested such a ridiculous idea. Phonetele's witnesses explicitly testified how, from inception, that the Phonemaster was designed and manufactured with its own, internal protective circuitry. Alone, such egregious errors in fact finding warrant a conclusion that the delay exceeding 4 years prejudiced Phonetele. When the trial court remembers nothing in respect to one of the critical issues, how can the decision be a fair and considered one?

their primary jurisdiction.

Phonetele I mandates that the antitrust court adhere rigorously to the prior regulatory authority. Phonetele I engrafted a requirement that the antitrust court strictly adhere to the regulatory authority; this "requirement" has been accomplished by including within the specific regulatory defense a test that the monopoly prove its conduct was necessitated by "concrete factual imperatives recognized as legitimate" by the FCC and CPUC. By its very language, therefore, Phonetele I incorporated the regulatory authority's treatment ("necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority") as the operative test of the regulated utility's affirmative defense. Indeed, Phonetele I's language setting forth the

Law of the Case is purposefully narrow and specific. In the case at bar, the courts below have erred by failing to apply the Law of the Case as its language clearly intended, a very specific test, which focused upon, and required, close relationship between ATT's purported good faith factual beliefs ("concrete factual imperatives" e. g. empirical facts), and the degree to which these imperatives "necessitated" defendants' conduct. The Circuit Court committed reversible error by (1) permitting generalized concepts of "economic" justification to creep in as pertinent to the affirmative defense, and (2) concluding as it did, that merely permitting the PCA tariff to remain in effect pending certification somehow meant that the regulatory authorities recognized the Bell System tariffs as legitimate. As

a practical matter, in 1981, if the court properly applied the Law of the Case, it was well-neigh impossible for ATT to prevail at trial against Phonetele.[11] At trial, ATT did not deny that the Bell System adamantly opposed certification in favor of its PCA tariffs. In fact, the Bell defendants proudly admitted to Bell's unyielding opposition to certification. Even at trial in 1984, the Bell witnesses testified one after another that the FCC registration program, enacted in 1975, was inadequate to protect the network, because it lacked adequate safeguards. In the broadest sense, the sole issue for trial

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[11]At trial, the trial court agreed with Phonetele that the regulatory opinions constituted "evidence" in the case under Evidence Code Rule 803(8)(c). These decisions, along with other evidence, constitute a formidable factual record which it was impossible for Bell to overcome if the lawsuit were fairly judged.

concerned whether the Bell System's zealous conduct in opposing certification as the regulators proposed -- and insisting upon its own brand of "all or nothing" certification -- was justified in accordance with the affirmative showing required of it by Phonetele I. Yet, Phonetele I ruled that ATT may not justify its actions based upon some mistake of law in interpreting FCC opinions. (p. 738).

The courts in the case at bar unwittingly allowed themselves to become immersed in technical questions involving electronics and telephony although such issues constitute the precise ingredients that regulators, not courts, deal with.[12]

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[12]The error in the case at bar is conspicuous. One need only read the Ninth Circuit opinion as it speaks of "high voltages", "excessive amplitude", "improper line balance", network harms, etc. to realize that the court has addressed throughout its opinion issues which repre-

Departure From Accepted and Usual Proceeding

Robert L. Feiner, Phonetele's President, filed Judicial Misconduct Complaints against two District Court Judges who had been assigned to the instant case. Mr. Feiner alleged serious appearances of impropriety. Phonetele II cited with approval language that "... remand might be proper if appellant made a convincing showing of prejudice". (p. A-19). Phonetele II concluded, among other things, that though Phonetele "was left with the impression that something is seriously wrong ..." that Phonetele has articulated no reasons to support its "impression". In taking over 4 years to

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sent classic primary jurisdiction issues. By wading into technical waters in which it has neither experience nor expertise, the District Court committed reversible error.

decide the case, the trial Judge violated The Code of Conduct for United States Judges, Canon 3A(5), "A judge should dispose promptly of the business of the court." Yet, there is more than the unexplained and unconscionable delay.

William French Smith ("Smith") was on the Board of Directors of PTT (defendant herein) until he resigned to become Attorney General of the United States. To fill a vacancy, Smith "appointed" the trial Judge who presided over Phonetele's trial. Earlier, in 1972, Smith had "appointed" the same Judge to the Los Angeles County Superior Court. While this trial Judge had the case at bar under submission, Smith resigned as Attorney General, and returned to the Board of Directors of PTT, thereby displacing one of his law partners who sat on the Board in Smith's absence.

Smith de facto never left the Board of PTT. Conclusion: a defendant appointed the trial Judge. The trial Judge also had a 28 year professional relationship (including law partners for about 12 years) with former 9th Circuit Judge Shirley Hufstedler, a member of the Board of Directors of a Bell System affiliate, U.S. West.

Canon 2A states in part that "A judge must avoid all impropriety and appearance of impropriety." Canon 3C says in part that "A judge shall disqualify himself or herself in a proceeding in which the judge's impartiality might be questioned. ..." Under the holding of Liljeberg v. Health Services Acquisition Corp., 486 U.S. 847, 108 S.Ct. 2194 (1988), misconduct such as Mr. Feiner alleged (a Judge proceeding under an appearance of con-

flict) alone warrants "vacatur" of the lower court's decision.[13] "The very purpose of §455(a) is to promote confidence in the judiciary by avoiding even the appearance of impropriety whenever possible." 108 S.Ct. at p. 2205). There is no misconduct attributed to Hufstedler or Smith; the sole misconduct relates to the trial Judge who should have recused himself.

In dismissing the Judicial Misconduct Complaints as "frivolous" on June 12, 1990, the Chief Judge of the 9th Circuit held that no "actual" impropriety was

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[13]A front page, column right lead article in the Los Angeles Daily Journal, on May 28, 1990, devoted 120 column inches to Mr. Feiner's judicial misconduct Complaints. A follow-up Page 3 article with a six column banner headline and totalling 30 column inches appeared on June 19, 1990. A third article, "Judicial Ethics and Other Fairy Tales" is pending publication in the Daily Journal.

shown. Yet, the Chief Judge failed even to address the "appearance" of impropriety although an "appearance" was clearly demonstrated. An appeal to the Judicial Council sustained the Chief Judge. Thereby, an extremely serious complaint that warranted "vacatur" under Liljeberg, is denigrated as "frivolous". There was no regard that "[t]he very purpose of §455(a) is to promote confidence in the judiciary by avoiding even the appearance of impropriety whenever possible." Id.

For the reasons set forth above, the Court should grant certiorari.

ARGUMENT

I. ATT FAILED TO JUSTIFY ITS MONOPOLIZATION

The national telephone network is an "essential facility". As such, the monopoly which owns it, the Bell System, must grant access on reasonable terms to its competitors. Otherwise, monopolization is proven. Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 105 S.Ct. 2848, 86 L.Ed.2d 467 (1985); Mid-Texas Communications Systems, Inc. v. ATT, 615 F2d 1372, 1387-88 (5th Cir. 1980). In respect to ATT specifically, the trial Judge in the government's case remarked, "It is clear, moreover, that otherwise innocent or ambiguous behavior may violate the Sherman Act when considered together with the remainder of the conduct." (524

F. Supp. at p. 1344). These basic tests of monopolization are well established. Therefore, on the facts of instant case, even assuming arguendo that Bell was motivated in part by network protection, antitrust liability would still be appropriate if otherwise predatory intent predominates.

Numerous cases hold that antitrust immunity may result where a sufficient regulatory coercion of the regulated monopoly's conduct is present so that a repugnancy will likely result if antitrust laws were applied. (see for example, United States v. National Ass'n of Sec. Dealers, 422 U.S. 694, 719-720, 95 S.Ct. 2427, 2442-43, 45 L.Ed.2d 486 (1975). However, it is not sufficient that anti-competitive conduct be merely "prompted" by the regulator. [Cal. Retail Liquor

Dealers Ass'n v. Midcal Alum., 445 U.S. 97, 104, 100 S.Ct. 937, 943, 63 L.Ed.2d 233 (1980)] Antitrust immunity may not be conferred when a regulator merely adopts a public utility's tariff. Cantor v. Detroit Edison Co., 428 U.S. 579, 598, 601-602, 96 S.Ct. 3110, 49 L.Ed.2d 1141 (1976).

Other than implied immunity, however, regulated monopolies are held to the same rules as any other monopoly. "[t]here is nothing unjust in a conclusion that respondent's participation in the decision is sufficiently significant to require that its conduct implementing the decision, like comparable conduct by unregulated businesses, conform to applicable federal law." Cantor, 428 U.S. at 594.

Therefore, while regulated status is a "fact of market life", the antitrust

courts have refused to modify the requisite standard of intent for regulated companies such as ATT. In regulated monopoly cases, the regulated entity may avoid antitrust immunity only if it can prove at trial that its conduct was "necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority." Phonetele I, at p. 738. Phonetele I has already declined ATT's request for immunity. What has been added to the record to support an innocent intent, a defense verdict, after trial? Where is the evidence which demonstrates that regulatory authority necessitated ATT's conduct? There is none. As a matter of law, ATT's "economic" arguments do not suffice; they are not even relevant to the issue of ATT's "intent".

To establish Section 2 liability,

specific intent is not required.[14] Economic arguments aside -- irrelevant as a matter of law -- ATT's only argument supporting its purported "innocent intent" depends upon its professed concern that interconnection could damage the network. Such a generalized concern, lacking an empirical basis as it did, was in fact expressly rejected by the FCC and CPUC. Therefore, "economic harm" arguments were not "recognized as legitimate".

The trial court's statements that the FCC's rulings merely decided that "registration was the best solution", underscore

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[14]The law is clear that a general intent will support the offense of monopolization under Section 2 of the Sherman Act. Aspen, supra., at p. 603, n.28, 105 S.Ct. 2857 n.28; California Computer Products, Inc. v. IBM, 613 F2d 727, 735 (9th Cir. 1979)

the court's error.[15]

II. THE CRITICAL INTERPLAY OF PRIMARY JURISDICTION

Antitrust cases against regulated monopolies almost invariably defer jurisdiction until the regulatory authority has decided the regulatory issues, such as certification, registration, etc. [Carter v. ATT, supra.; Macom Products Corp. v. ATT, 359 F. Supp. 973 (C.D. Cal. 1973); Chastain v. ATT, 351 F. Supp. 1320 (D.C.

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[15]In reference to PCAs, on one hand, and a system of standards on the other, the appellate court stated that "Two means of preventing harm to the network were readily apparent." This statement is incredibly naive. Any attempt to legitimize PCAs as one means to prevent harm to the network means nothing more than to say that ATT advocated PCAs and, early on, for a short while, PCAs were tolerated by the regulators as one means to protect the network pending a system of engineering standards. No regulatory imprimatur ever attached to PCA tariffs.

1972)] In the regulatory background of the case at bar, the regulators exercised primary jurisdiction for many years while technical/economic aspects of more liberalized interconnection were studied by the agencies, mainly the FCC and CPUC.

The FCC pre-empted the field and enacted its registration program in 1975. [see Telerent Leasing Corp., 45 FCC2d 204 (1974)] Thereafter, ATT attacked the FCC's registration decisions (the FRO and SRO) through the courts. Thereby, ATT delayed the implementation of the FCC Registration Program for two more years until late 1977. [see North Carolina Util. Comm'n v. FCC, 537 F2d 787 (4th Cir. 1976), cert denied, 429 U.S. 1027 (1976); 552 F2d 1036 (4th Cir. 1977), cert denied 434 U.S. 874 (1977)]. The Honorable Judge Tuttle observed in rejecting ATT's

opposition to the FCC's registration program, "... what petitioners are attempting is the preservation of the carrier's lawmaking authority over independent manufacturers." North Carolina, supra., 552 F2d at 1051, emphasis is the court's. Also, "The unreasonableness and discriminatory effect ... of the present 'connecting arrangement' tariff is established and is not challenged on this appeal." 552 F2d at 1055.

Among the important decisions made by the FCC is the relegation of "economic" issues to Docket 20003, a separate case from Docket No. 19528, which considered only the technical, engineering, operational and administrative aspects of registration. (see FRO, 56 FCC2d at 596-97, 600-601). ATT had been unable to convince the FCC that registration should

be delayed until all the myriad economic implications of competition could be assessed. This well documented regulatory history, underscores the trial and appellate court's error in insinuating economic concerns about competition into the equation for determining ATT's "intent".

III. STANDARD OF REVIEW; DE NOVO

Phonetele realizes that this Court does not customarily concern itself with factual findings. However, because the District Court's findings are pervasively flawed, a brief discussion on the factual issues follows. The record in the instant case contains a great deal of Phonetele's evidence represented by Bell System written admissions via contemporaneous documents, letters and memoranda. No evidence could be more trustworthy to prove intent.

In contrast, a scant portion of ATT's evidence is contemporaneous with the events in question. Most of the Bell evidence consists of prepared direct examination which the District Court permitted, over Phonetele's vigorous objection, in a written form. Little of the Bell System evidence involves contemporaneous documents.

An important refinement respecting the standard of review should properly come into play in this type of case, a documents case.[16] This Court has ruled that an appellate court is empowered to set aside "clearly erroneous" findings. United States v. United States Gypsum Co.,

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[16]The Circuit Court did not delve into this refinement at all. The Annotations which were filed shortly after oral argument would have assisted the court, so that a United States Gypsum type of review would have been quite feasible and appropriate.

333 U.S. 364, 393-399, 68 S.Ct. 525, 92 L.Ed. 746 (1948). A finding is "clearly erroneous" when although there is evidence to support it, the reviewing court is left with the definite and firm conviction that a mistake has been committed." 333 U.S. at 395. In United States Gypsum, the government relied largely upon document evidence as does Phonetele. "Where such testimony is in conflict with contemporaneous documents we can give it little weight, particularly where the crucial issues involve mixed questions of law and fact." (at p. 396). The court in United States Gypsum, reversed and found conspiracy on the question whether licenses "show plainly a conspiracy to violate the Sherman Act." (at p. 400). Also, interpretations of regulatory decisions, of critical importance to the case at bar, involve only

questions of law, judged de novo on appeal. 5A Moore's Federal Practice, para. 52.03[2]; see also Dunn v. Phoenix Newspaper, 735 F2d 1184, 1186 (9th Cir. 1984). Phonetele II failed to conduct any de novo review. Instead of de novo review, the appellate court blithely dealt with the central issue in the case by accepting the following at face value:

> The CPUC found that direct connection of the Phonemaster could endanger equipment and disrupt signal transmissions in identifiable ways, and both the CPUC and the FCC considered the PCA to be a reasonable, properly focused mechanism to prevent such harms from occurring. (at p. A-13)

As a matter of law, decided in the exercise of primary jurisdiction, the regulatory authorities had already thoroughly discredited the very conclusion which the courts below embraced.

The trial court devoted one short paragraph in its opinion (p. 73) to

dispose of Phonetele's cause of action for intentional interference with prospective economic advantage. The Circuit Court failed to address the issue at all. A recent case, which Phonetele cited to the Circuit Court, held that de novo review by the reviewing court is appropriate when state issues were involved. [Salve Regina College v. Russell, 111 S.Ct. 1217, 113 L.Ed.2d 190 (1991)]. Thus, by declining any meaningful review at all, much less de novo review, the Circuit Court abdicated its responsibility and committed reversible error.

It is also noteworthy that on virtually identical facts and regulatory background, the District Court in Oregon granted partial summary judgment and collateral estoppel against the Bell System -- e. g. liability as a matter of

law -- the very month the Phonetele case began trial, June, 1984. (see Selectron, Inc. v. ATT, 587 F. Supp. 856 (D. Ore. 1984), relying on Litton)

CONCLUSION

In the years 1968-1977, the Bell System unlawfully dictated national communications policy for the United States. For reasons unknown, the trial court's opinion heavily labored to find justification where none really existed. At the same time, ATT, not Phonetele, bore the burden of proof. The Circuit Court's perfunctory reasoning in Phonetele II suggests that the judiciary felt compelled to deliver the coup de grace to what it view as a "tired" piece of litigation. What has Phonetele proven? Through its tariff power, the Bell System exer-

cised almost absolute control over the telephone terminal equipment market. The PCA tariffs were unlawful, discriminatory and restrictive as found by both the CPUC and FCC. Predatory intent, cognizable under Section 2, has been well proven. Nevertheless, the legal issue is whether, given predatory intent, ATT proved its regulatory defense (a regulatory imperative or necessity justifying its conduct) notwithstanding the prima facie case against it.

On what basis did the courts below infer innocent intent? Phonetele asks this Court to articulate a critical analysis test in order to prevent regulated utilities from injecting wide-ranging "regulatory" issues into the considerations surrounding a regulated monopoly's justification of its conduct.

The concept of Section 2 "General intent" lacks precision conducive to practical application of the regulated monopoly antitrust defense. This is particularly true in that the Law of the Case which mandates a very specific analysis, probing the question of regulatory necessity. As the case at bar illustrates, a monopolist might prevail in such cases if it can convince the finder of fact that it acted with "some" regulatory justification. However, it makes no sense if "some" regulatory justification simply means only that some regulatory explanation or nexus -- even if not "compelling" of the monopolistic conduct -- would suffice. Unless the antitrust defendant is required to demonstrate that its actions were "compelled" in some meaningful fashion by the regulatory authority, the

justification becomes an unintended formidable shield for the regulated monopolist.

Phonetele suggests that the finder of fact employ the following test in regulated monopoly cases in determining "intent": (1) the monopolist demonstrate that innocent intent predominates in mixed intent cases. (for example, a 40% showing of innocent intent lacks justification), and (2) the specific regulatory imperative must be identified in respect to the precise conduct subject to the justification defense. Gross generalities, or irrelevant regulatory issues, will otherwise cloud the court's judgment as happened in the case at bar. The suggested refinement to Justice Kennedy's regulated monopoly's justification defense is altogether appropriate, even necessary. Otherwise, the justification defense will

lead to bad results in regulated monopoly cases. At the same time, the suggested refinement will safeguard plaintiffs to ensure a principled analysis in accordance with the regulated monopoly's affirmative defense.

The opinions below unmistakably suggest that litigation transversing 18 years is simply too old, too outdated, to merit serious attention. Phonetele asks this court to intervene so that its action will not be further "swept under the rug". Phonetele's story is so compelling that the Justice Department called Mr. Feiner as the United State's first witness in the divestiture case against the Bell System. If anything, Phonetele's significant place in the forefront of interconnect litigation and the length that this litigation has been pending entitle Phonetele to a

special dispensation by this Court.

Issues important in the administration of justice are well-presented by the instant Petition. The Law of the Case has been utterly ignored, certainly breached. The question of mixed motivation for monopolistic behavior represents a case of first impression. The question of the delay represents a case of first impression. The treatment of the evidence at trial was pervasively in error so that one is "... left with the definite and firm conviction that a mistake has been committed". The ethical questions presented also raise substantial doubt about the appearance of impropriety.

A grant of Petition would renew the faith of many in our system of justice. It would also well serve the ends of the administration of justice by ad-

dressing several questions important to the conduct of antitrust lawsuits, particularly those prosecuted against regulated monopolies.

Dated: January 24th, 1992

Respectfully submitted,

Rick M. Stein
Attorney for Petitioner
Phonetele, Inc.

APPENDIX A

SPECIAL EARTHQUAKE NOTICE

This opinion is being filed while the Clerk's office in San Francisco is closed due to severe earthquake damage. Once the Clerk's office is operational, notices will be placed in legal newspapers throughout the Circuit. At that time parties may seek additional time to file a petition for rehearing if they desire to file one.

FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PHONETELE, INC., *Plaintiff-Appellant,* v. AMERICAN TELEPHONE & TELEGRAPH COMPANY, et al., *Defendants-Appellees.*	No. 88-6353 D.C. No. CV-74-3566-HLH OPINION

Appeal from the United States District Court
for the Central District of California
Harry L. Hupp, District Judge, Presiding

Argued and Submitted
August 11, 1989—Pasadena, California

Filed November 6, 1989

Before: Betty B. Fletcher and Dorothy W. Nelson, Circuit Judges, and Philip M. Pro,* District Judge.

Opinion by Judge Fletcher

*Hon. Philip M. Pro, United States District Judge for the District of Nevada, sitting by designation.

SUMMARY

Antitrust

Affirming a judgment of the district court, the court held that telephone interconnection restrictions do not violate antitrust laws if the regulated common carrier can justify the restrictions.

Appellant Phonetele manufactures and sells the Phonemaster, a device known as a call restrictor, connected between a telephone and the rest of the telephone network to prevent the user from placing calls beyond a predetermined area. Originally the Bell System had complete responsibility for the operation of the telephone system and ownership of all telephone equipment. The Federal Communications Commission in its *Carterfone* decision, *Use of Carterfone Device in Message Toll Telephone Service*, 13 F.C.C.2d 420 (1968), opened up the possibility of a great many manufacturers designing and selling equipment to be attached to the network. Two means of preventing harm to the network were readily apparent. One was to require protective connecting arrangements (PCAs), the option selected by AT&T, and the other was to develop standards for interconnecting attachments. In late 1970, Phonetele was preparing to market the Phonemaster in California and notified AT&T of the need for a PCA. A special PCA, designated ZZAGM, was designed for and delivered to Phonetele in 1971. However, Phonetele at some point adopted the position that a PCA was unnecessary and that Phonemaster could be connected directly without harm. When Phonetele made a connection directly into the network, General Telephone sought to disconnect as did PT&T. The California Public Utilities Commission ruled the PCA equipment valid, and the Supreme Court reversed the CPUC's decision that the PCA was necessary to prevent harm. In 1975, the CPUC issued an Order which permitted the direct connection of certified devices, later stating that

PCAs were not needed to prevent actual or probable harm to the telephone network.

[1] Phonetele's appeal challenged AT&T's conduct in the years between *Carterfone* and the adoption of the registration programs, alleging that AT&T's opposition to registration and insistence on PCAs during that period were intended to prevent Phonetele from entering or succeeding in the market. AT&T argued conversely that its concern was to protect the quality of the market. [2] The district court found that, in enacting its tariffs, AT&T was acting on the basis of its reasonable belief as to how best to provide effective telephone service to the public, based on technical imperatives known to it and recognized as legitimate by the regulating authorities. This finding is not clearly erroneous in light of the regulatory history. The CPUC found that direct connection of the Phonemaster could endanger equipment and disrupt signal transmissions in identifiable ways, and both the CPUC and the FCC considered the PCA to be a reasonable, properly focused mechanism to prevent such harms from occurring. [3] Phonetele also argued that AT&T and the local operating companies acted unreasonably in applying tariffs to the Phonemaster, but none of Phonetele's arguments in this regard had merit. [4] During the CPUC proceedings, the CPUC entered an order, never changed, that local companies could not charge for the use of the ZZAGM, and as a result, for much of the relevant time, Phonetele's customers did not have to pay for the ZZAGM. [5] The ZZAGM was not approved for nationwide use because AT&T determined it did not provide sufficient protection against blockage and glare, and [6] Phonetele argued that it was thus required to use a defective, not merely unnecessary, PCA. This argument was rejected on the grounds that Phonetele's customers did not have to pay for the ZZAGM, and the ZZAGM did protect against other major harms. Phonetele cited no evidence that any of its customers ever complained about their Phonemaster because of longitudinal imbalance.

COUNSEL

Rick M. Stein, Sanger & Stein, Palm Springs, California, for the plaintiff-appellant.

George L. Saunders, Jr., Sidley & Austin, Chicago, Illinois, for the defendants-appellees.

OPINION

FLETCHER, Circuit Judge:

Phonetele, Inc. appeals the judgment of the district court in favor of AT&T and related defendants (hereafter referred to collectively as "AT&T") on Phonetele's antitrust causes of action. Phonetele's principal claim on appeal is that the district court could not have found, on the evidence presented to it, that AT&T had carried its burden of proof on its affirmative defense of regulatory justification. Phonetele also argues that the district court erred in defining the relevant market, and that Phonetele was deprived of a fair trial because the district court delayed its decision for four years. We affirm.

I. FACTS

Phonetele manufactures and sells the "Phonemaster." The Phonemaster is a device of the type known generically as a "call restrictor," connected between a telephone and the rest of the telephone network to prevent the user from placing calls beyond a predetermined area. Its primary market consists of medium-to-large companies with numerous telephone extensions. The Phonemaster allows the company to restrict phone usage by employees or customers. It is a sophisticated device that not only can prevent unauthorized long-distance calls, but also can allow the company to designate exceptions, for example allowing employees to make long-distance calls only to certain area codes or prefixes.

This dispute first came before us in *Phonetele, Inc. v. AT&T*, 664 F.2d 716 (9th Cir. 1981)(*Phonetele I*), where we reversed the district court's dismissal of Phonetele's complaint.[1] We held that, although the defendants' status as regulated common carriers did not confer antitrust immunity on them, an affirmative defense based on the realities of regulation was available to them:

> While a given regulatory scheme may not amount to the degree of necessity required to confer implied immunity on all activities of a regulated entity, some degree of necessity may be established as a matter of fact in individual cases. When the regulated entity assertedly attempts to respond to its duties as a common carrier by filing and implementing an anticompetitive tariff, the antitrust laws do not apply to the tariff without regard to the technical and legal constraints flowing from the regulatory structure. *If a defendant can establish that, at the time the various anticompetitive acts alleged here were taken, it had a reasonable basis to conclude that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority, then its actions did not violate the antitrust laws.* At this stage in the proceedings, *it appears this inquiry will depend largely on whether the facts show the companies did reasonably conclude, given their expertise, that uncontrolled NCSU* [Network Control Signal Unit[2]] *interconnection would endanger their own equipment or disrupt their own signal transmissions*

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[1]The district court had dismissed on the grounds that the FCC and state utilities commissions had exclusive jurisdiction and that the Communications Act of 1934, 47 U.S.C. §§ 151-609, conferred an implied antitrust immunity on the defendants' activities. *Phonetele I*, 664 F.2d at 721.

[2]Network control signaling consists of the transmission of signals to perform functions such as call supervision, dialing, called number identification, and audible tone signals. The Phonemaster is one type of NCSU.

> *in identifiable ways, and also that the tariff as filed was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such real harm from occurring.*

664 F.2d at 737-38 (emphasis added). The district court assumed throughout this case, and AT&T does not dispute, that AT&T's restrictions on interconnection would be an antitrust violation unless AT&T could justify the restrictions.

Phonetele's appeal accordingly focuses on AT&T's conduct in seeking, opposing and implementing various regulatory measures directly affecting the Phonemaster. A brief history of telephone regulation as it relates to such "ancillary" devices[3] is therefore necessary for an understanding of this case.

The Bell System originally had complete responsibility for the operation of the telephone system and ownership of all telephone equipment, including the user's telephone itself. Tariffs existed prohibiting the attachment of any non-Bell equipment to the network. In 1947, the Federal Communications Commission (FCC) allowed recording devices to be physically attached to the telephone line on the condition that the equipment necessary to make such physical connection was provided, installed, and maintained by the Bell System. *Use of Recording Devices*, 11 F.C.C. 1033 (1947). Then, in 1968, the FCC entered its *Carterfone* decision. *Use of the Carterfone Device in Message Toll Telephone Service*, 13 F.C.C.2d 420 (1968). That decision announced a broad holding:

> [A] customer desiring to use an interconnecting device to improve the utility to him of . . . the telephone system . . . should be able to do so, so long as

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[3] An ancillary device is one, like the Phonemaster, which is attached to the telephone network but does not replace any component of that network.

> the interconnection does not adversely affect the telephone company's operations or the telephone system's utility for others. A tariff which prevents this is unreasonable. . . .
>
> There has been no adequate showing that non-harmful interconnection must be prohibited in order to permit the telephone company to carry out its system responsibilities. . . . We are not holding that the telephone companies may not prevent the use of devices which actually cause harm, or that they may not set up reasonable standards to be met by interconnection devices. These remedies are appropriate; we believe they are also adequate to fully protect the system.

13 F.C.C.2d at 424.

AT&T was invited to file new tariffs. It responded with new tariffs providing that permission to attach ancillary equipment was conditioned upon attachment through a "connecting arrangement" to be supplied by AT&T. The FCC allowed these tariffs to go into effect without hearing or investigation but refused to approve them expressly. *American Telephone and Telegraph Co. "Foreign Attachment" Tariff Revisions*, 15 F.C.C.2d 605, 610 (1968).

The FCC appears to have taken this somewhat ambivalent position because of the novelty of its policy requiring the Bell System to permit interconnection. Interconnection posed technical and economic problems of considerable complexity. *Carterfone* opened up the possibility of a great many manufacturers designing and selling equipment ~~to~~ be attached to the network. The FCC therefore implemented a study period. Two means of preventing harm to the network were readily apparent. One was to require protective connecting arrangements (PCAs), the option selected by AT&T. The other was to develop standards for interconnecting attachments. This

latter option had several problems. Either AT&T would have had to set standards and ensure compliance itself (an option subject to anticompetitive problems), or else a federal bureaucracy would have been required to do so.

The FCC requested the National Academy of Sciences (NAS) to review the technical problems of interconnection and to make recommendations. The NAS issued its report in June, 1970. This report identified four general types of harm which could result from the electrical connection of ancillary devices: (1) dangerously high voltages;[4] (2) excessive amplitude;[5] (3) improper line balance;[6] and (4) improper control signals.[7] The NAS concluded that PCAs were a technically acceptable way to prevent these harms from occurring. It also concluded that a registration program would be effective only if it provided for approval of designs, certification of installation methods, testing of equipment, and oversight of maintenance.

The FCC next commissioned a consultant's report on the practical methods by which the NAS recommendations could be implemented. This report was critical of the time, expense, and effort needed to implement a registration program as envisioned by the NAS. Nevertheless, the FCC began studying the possibility of a standards approach for certain types of

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[4]Most household appliances use 110 voltage, but the telephone system uses considerably less. Most devices intended to be connected to the telephone system, including the Phonemaster, use 110 voltage. Telephone lines must be protected from the accidental entry of 110 voltage, because such voltages could result in the death of telephone line workers.

[5]Signals of excessive amplitude can leak into neighboring telephone lines causing noise and cross talk.

[6]Improper line balance results from the introduction of a higher current into one side of the line than the other. This, too, produces interference on other lines.

[7]Control signals direct calls to their intended destination. Improper control signals can cause various problems, including misdirection of calls.

equipment. It started with a device called the PBX.[8] Phonetele asked the FCC to study a standards program for call restrictors, but the FCC declined to do so.

By 1972, it became apparent that the FCC was leaning towards adopting a streamlined registration system without certification of installation, testing or maintenance. AT&T was bitterly opposed to such a system, and openly expressed its opposition. AT&T decided to continue the PCA requirement and to resist the imposition of a streamlined registration program.[9]

In 1975, the FCC proposed a comprehensive new registration program. *Proposals for New or Revised Classes of Interstate and Foreign Message Toll Telephone Service (MTS) and Wide Area Telephone Service (WATS)—First Report and Order*, 56 F.C.C.2d 593 (1975), *modified in part*, 57 F.C.C.2d 1216 (1976), *aff'd sub nom. North Carolina Util. Comm'n v. FCC*, 552 F.2d 1036 (4th Cir.), *cert. denied*, 434 U.S. 874 (1977). Under this program, the FCC would set standards for all ancillary electrical devices. The Phonemaster was regis-

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[8]A PBX is a Private Branch Exchange, a switching mechanism located on the premises of the telephone customer, through which calls to and from extension telephones are funneled.

[9]As previously indicated, any registration system required the cooperation of the FCC, in that it was clear that registration would need to be performed by a body other than AT&T. AT&T was not in a position to enact registration unilaterally, although it was of course in a position to argue more forcefully in favor of a suitable registration system. The district court found that AT&T did not oppose registration until it became clear it could not achieve the sort of registration program it deemed necessary. The district court specifically found that this opposition was not a "sham" engaged in for purposes of delay, and, therefore, was shielded from antitrust liability by the *Noerr-Pennington* doctrine. *See Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); *United Mineworkers v. Pennington*, 381 U.S. 657 (1965). *See also California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508 (1972) (finding that appellees efforts to harass and deter respondents in their use of administrative and judicial proceedings came within the "sham" exception of the *Noerr* case).

tered under this program, and since that time it has not been necessary to install a PCA in order to use a Phonemaster.

Meanwhile, proceedings directly involving the Phonemaster were taking place before the California Public Utilities Commission (CPUC). Phonetele was preparing to market the Phonemaster in California in late 1970. It notified AT&T of the need for a PCA. A Bell Labs engineer, under time pressure from Phonetele, designed a PCA, which was denominated the CTD. A schematic drawing was delivered to Phonetele in March 1971. Phonetele indicated the PCA was suitable. The CTD was used only by the Pacific Telephone and Telegraph Company ("PT&T") in California, where it was redenominated the ZZAGM.[10] At some point Phonetele adopted the position that a PCA was unnecessary and that the Phonemaster could be connected directly without harm.

Clashes soon arose in the territory of General Telephone Company of California ("General Telephone") when Phonetele made a connection of the Phonemaster directly into the network. General Telephone sought to disconnect. The matter was presented to the CPUC. The CPUC ordered General Telephone to allow direct interconnection. Phonetele then adopted the same position in the territory of PT&T, which resulted in additional litigation before the CPUC. Phonetele refused to test the ZZAGM with its equipment. In November 1971, the CPUC ruled that the PCA requirement was valid, reversing its prior order to General Telephone. In *Phonetele, Inc. v. General Telephone Co. of California*, Interim Opinion and Order, Cases No. 9177 & 9265 (1972), the CPUC found that the Phonemaster as it then existed had the potential to

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[10]Phonetele argues that the change in designation of the PCA from "CTD" to "ZZAGM" was intended to conceal the fact that the CTD/ZZAGM harmed the network. Phonetele offers no evidence to support this allegation. The district court found that the change in name was nothing more than the result of different nomenclature employed by PT&T and AT&T.

cause crosstalk and excessive noise on the network, misdirected telephone calls, improper billings, and high voltage. The CPUC concluded from the existence of these potential harms that General Telephone's PCA requirement was reasonable, until such time as a certification program was implemented. In a subsequent decision by the CPUC, the utilities were ordered to supply the PCA to Phonetele customers without charge. *See Phonetele, Inc. v. Publ. Util. Comm'n,* 11 Cal.3d 125, 127 n.1, 113 Cal. Rptr. 16, 520 P.2d 400 (1974).

Upon review of the CPUC decision, the California Supreme Court reversed the CPUC's decision that the PCA requirement was "necessary" to prevent harm to the telephone system because the CPUC had applied the wrong standard. *Phonetele,* 11 Cal.3d at 128. The California Supreme Court did not, however, hold that the Phonemaster could be directly connected to the telephone network, or that certification was necessarily preferable to a PCA requirement. According to the Supreme Court, the CPUC should have asked whether the evidence demonstrated that the Phonemaster would have an *actual* or *probable* (as opposed to *possible*) adverse effect upon the telephone system. 11 Cal.3d at 129-30. The Supreme Court continued in effect the CPUC's order requiring utilities to supply the protective devices free of charge until the Commission reconsidered the evidence in light of the proper standard or implemented a certification program. 11 Cal.3d at 132-33.

In April, 1975 the CPUC issued an Order which, like the FCC program, permitted the direct connection of certified devices. This decision became final in May, 1976. In 1977, the CPUC ruled that PCAs were not necessary to prevent actual or probable harm to the telephone network. *Order Denying Rehearing and Stay Modifying Decision No. 87620,* Decision No. 87920, Case No. 9625 (1977).

II. DISCUSSION

A. *Standard of Review*

The standard of review of a regulatory justification defense has not yet been decided by this circuit. We referred to the defense in *Phonetele I* as a "factual justification[]," to "be established as a matter of fact in individual cases," 664 F.2d at 737-38. The closely related question of whether there was a business justification for an alleged tying arrangement was submitted to the jury in *Mozart Co. v. Mercedes-Benz of North America, Inc.*, 833 F.2d 1342, 1350-51 (9th Cir. 1987), *cert. denied*, 109 S.Ct. 179 (1988). We reviewed to see whether there was substantial evidence to support the jury's verdict. *Id.* We conclude that regulatory justification as a defense to a monopolization claim similarly should be viewed as a factual inquiry and the district court's determination reviewed by us under the clearly erroneous standard. Phonetele also argues that specific facts found by the district court are incorrect or lack support in the record. We review such arguments under the clearly erroneous standard. Fed. R. Civ. P. 52(a). This rule applies equally to facts found from a written record. *Id.*

B. *Sufficiency of the Evidence*

[1] Phonetele's appeal challenges AT&T's conduct in the years between *Carterfone* and the adoption by the FCC and the CPUC of registration programs. Phonetele alleges that AT&T's opposition to registration and insistence on PCAs during this period was intended to prevent Phonetele from entering or succeeding in the market. AT&T argues, conversely, that its concern was to protect the quality of the telephone network.

The district court rejected Phonetele's contention that AT&T acted unreasonably in not establishing a certification program for call restrictors. The district court relied on the fact that the FCC was studying the feasibility of a certifica-

tion program in a more deliberate manner, and in doing so was following the recommendation of the NAS. In light of the fact that the FCC and CPUC both permitted the requirement of PCAs pending the creation of a certification program, the district court's conclusion that AT&T acted reasonably was not clearly erroneous. That the FCC and CPUC subsequently decided that registration was the best solution to the interconnection problem does not prove that AT&T's PCA requirement was *unreasonable* prior to those decisions.

The district court read our opinion in *Phonetele I* as leaving open a central issue in this case: whether the problem of interconnection and the filing of tariffs was to be viewed "from the standpoint of dangers to the system from the interconnection of unknown multitudes of electrical equipment," *Excerpt of Record* 66, or from the standpoint of the Phonemaster considered on its own. The district court concluded that the relevant inquiry in determining whether AT&T's tariffs were reasonable should focus on whether "ancillary equipment of a particular type poses dangers to the telephone system," rather than "whether a particular manufactured device necessarily poses such dangers." *Id.* The "particular type" relevant to this case was deemed to be "telephone call restriction equipment in general." *Id.* Phonetele does not challenge this conclusion.

[2] The district court found that, in enacting its tariffs, AT&T was acting on the basis of its reasonable belief as to how best to provide effective telephone service to the public, based on technical imperatives known to it and recognized as legitimate by the regulating authorities. This finding is not clearly erroneous in light of the regulatory history described above. The CPUC found that direct connection of the Phonemaster could endanger equipment and disrupt signal transmissions in identifiable ways, and both the CPUC and the FCC considered the PCA to be a reasonable, properly focused mechanism to prevent such harms from occurring. True, the California Supreme Court vacated the CPUC's ruling and invited the Commission to investigate the harms further, but

even during this period, when the need for a PCA in conjunction with the Phonemaster was in doubt, the local operating companies were permitted to require PCAs to be used, as long as they were provided to the customer free of charge. As a result, even if AT&T was not reasonable in believing PCAs to be *necessary* with the Phonemaster after the California Supreme Court's remand, Phonemaster cannot demonstrate any injury resulting from the PCA's continued use. Although Phonetele's position ultimately prevailed both before the FCC and before the CPUC, the test we articulated in *Phonetele I* only requires the defendant to establish that its conclusion "that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority" was *reasonable* at the time its conclusion was reached. *Phonetele I*, 664 F.2d at 737-38. AT&T was specifically permitted by the regulatory agencies to require a PCA to be used with the Phonemaster during a period when those agencies had not yet resolved the dispute between the merits of certification and protective devices. Until the issue was actually decided against PCAs, AT&T acted reasonably in requiring a PCA.

[3] Phonetele also argues that AT&T and the local operating companies acted unreasonably in applying the tariffs to the Phonemaster. None of Phonetele's arguments in this regard have merit.

[4] During the CPUC proceedings, the CPUC entered an order, never terminated, that the local operating companies could not charge for the use of the ZZAGM. As a result, for much of the relevant time period Phonetele's customers did not have to pay for the ZZAGM, and indeed could have benefitted from additional savings because Phonetele did not have to include duplicative protective circuitry in the Phonemaster itself.[11] Thus, as the appropriateness of requiring a

[11]It is unclear whether this cost savings was in fact passed on to Phonetele's customers. It is also unclear by how much the cost of the Phonemaster was or could have been reduced.

PCA to be used with the Phonemaster began to be cast in doubt, the costs of that requirement were imposed on the utilities, minimizing any harm to Phonetele.

[5] The ZZAGM was not approved by AT&T for nationwide use because AT&T determined that the ZZAGM did not provide sufficient protection against "blockage" and "glare."[12] The district court found that blockage and glare could degrade the quality of telephone service. The ZZAGM did not protect against these problems because the Bell Labs engineer responsible for the ZZAGM assumed that Phonetele would supply a delay to eliminate glare and did not recognize the blockage problem. In addition, between 1971 and 1974 the ZZAGM failed to correct longitudinal imbalance,[13] and in fact added to the problem. This problem was the indirect and unintentional result of disagreement between PT&T and Phonetele over the number of prongs to be used in the Phonemaster's plug. The ZZAGM was originally designed for use with a six-pronged Phonemaster, but was converted to four-prong use when Phonetele insisted on a four-prong plug. It was during this conversion that an engineering error was made, creating the longitudinal imbalance problem.

[6] Phonetele argues that it was thus required to use a *defective*, not merely unnecessary, PCA. The district court rejected this argument on the grounds that Phonetele's customers did not have to pay for the ZZAGM, and the ZZAGM did protect against other major harms, especially high voltage and excessive amplitude. While it would be irrelevant that

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[12]Blockage and glare are technical problems specifically associated with call restriction devices, which operate by opening and closing telephone lines. If the timing is not right, incoming calls can inadvertently be blocked by the device; this is called "blockage." If the line is closed before the user hangs up, incoming calls can be sent to the wrong extension, this is called "glare." These problems are endemic to the Phonemaster but can be minimized by careful timing of the disconnecting sequence.

[13]Longitudinal imbalance can result in noise on the telephone lines of other users.

the ZZAGM was provided free of charge if it in fact degraded the quality of Phonetele's product, the district court's finding that the ZZAGM was not on balance harmful, but rather did more good than harm, is not clearly erroneous. Also, that the one problem added by the ZZAGM, longitudinal imbalance, affected only the lines of other users rather than the lines of the Phonemaster user, suggests that the utilities were harming themselves more than Phonetele by failing to correct the longitudinal imbalance problem. Phonetele cites no evidence that any of its customers ever complained about their Phonemaster because of problems associated with longitudinal imbalance.

On the national level, AT&T continued to develop the original CTD, achieving an improved final version in 1972.[14] The final CTD was designed to be used with a variety of call restricting equipment, including but not limited to the Phonemaster. The district court found that the final CTD was ready for use before Phonetele was ready to enter the national market.[15] Phonetele, however, insisted at that time that if a PCA were to be required, it was under no obligation to accommodate its product to a general purpose PCA. The final CTD worked with the Phonemaster except for one wrinkle: the Phonemaster was designed to inform the telephone user that a call was restricted with the opening four-note motive from Beethoven's Fifth Symphony; the final CTD required the substitution of a dial tone or busy signal.[16] In the face of

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[14]This version will be called the "final CTD" to distinguish it from the ZZAGM.

[15]Phonetele asserts that the final CTD never actually existed and was never made available for testing with the Phonemaster. This assertion is directly contradicted by one of Phonetele's own memoranda, introduced at trial, discussing the final CTD's compatibility with the Phonemaster.

[16]The final CTD was also not usable behind "key systems," smaller systems which did not comprise more than a minimal portion of Phonetele's market because of the expense of the Phonemaster.

Phonetele also argues that AT&T's pressure for it to build a 1.5 second time delay into the Phonemaster, in order to reduce the problems of block-

Phonetele's opposition to the final CTD, AT&T designed two new PCAs specifically for the Phonemaster, one which was used when a Phonemaster was sold to the New York Times in 1974, and a second, never needed, to be used behind key systems. The district court's finding that Phonetele was not delayed in entering the national market by AT&T's failure to have a compatible PCA ready was not clearly erroneous.

Phonetele also argues that PT&T obtained favorable rulings from the CPUC by presenting its case before that commission fraudulently. The district court found that PT&T did not act fraudulently, and Phonetele does not cite to this court any evidence which would persuade us that the district court's finding in this regard was clearly erroneous.

C. *Written Testimony and Delay in Decisionmaking*

Phonetele argues that the district court's permission to both sides to use direct written testimony, in combination with the court's delay of almost four years in reaching its decision, requires reversal. According to Phonetele, AT&T's written direct testimony "assumed an importance far eclipsing the testimony of live witnesses and substantial documentary evidence presented by Phonetele" as the years passed and the district judge's memory dimmed. Appellant's Brief at 54. Phonetele concedes, however, that its own exhibits and recorded transcripts of its own evidence were available to the district court, reducing its claim to the argument that AT&T's evidence was prejudicial simply because it was in some way

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age and glare, was undertaken in bad faith. However, Phonetele argues only that the Phonemaster worked without such a delay; it does not cite evidence that use of a 1.5 second delay would not have helped prevent network harm. PT&T in fact allowed the Phonemaster to be installed without the 1.5 second delay. Phonetele's argument also suffers from an internal contradiction: in opposing the 1.5 second delay, Phonetele was resisting AT&T's attempts to suggest or impose standards, despite Phonetele's litigation position that standards rather than PCAs were the proper protective solution.

clearer or more easily accessible than Phonetele's testimony. Because Phonetele was also given the opportunity to present its direct testimony in written form, we fail to see how any prejudice resulting from the relative lack of clarity of the record created by Phonetele at trial can in any way be blamed on the ruling of the district court.

The use of written testimony is an accepted and encouraged technique for shortening bench trials. *Malone v. U.S. Postal Service*, 833 F.2d 128, 133 (9th Cir. 1987), *cert. denied*, 109 S.Ct. 59 (1988)(upholding district court's authority to *compel* written testimony). Although Phonetele argues it was prejudiced by AT&T's use of written testimony because AT&T had obtained valuable experience from litigating prior antitrust cases, Phonetele could have made an attempt to close this experience gap by reviewing those prior cases itself. More importantly, even if Phonetele could not realistically have undertaken such a review, Phonetele had the undisputed benefit of five days prior notice of what AT&T's direct testimony would be, presumably making it easier for Phonetele to cross-examine AT&T's witnesses.

Nor is our conclusion affected by the district court's delay in rendering its decision. We are appalled by the delay, but we are aware of no case holding that a district court commits reversible error by taking too long to decide a case. Indeed, we doubt that appellate review could ever be an effective means of enforcing district court timeliness. On appeal, this court may take one of three actions: affirm the district court's decision, remand to the district court to reconsider or explain its decision, or reverse the district court's decision. To vacate and remand a decision which the district court has spent several years crafting hardly seems a sensible means to reduce delay. To reverse the decision on the ground of delay would require us to presume that lengthy deliberation inevitably leads to mistake. Phonetele suggests that the district court's delay is evidence of its disinterest in or ignorance of the case. Although we do not condone the long delay, we are not willing

to assume without strong independent support that the district court departed from its proper role and considered only the evidence that was easiest to recall. *But cf. Ciccarello v. Graham*, 296 F.2d 858, 860 (5th Cir. 1961)(but noting that remand might be proper if appellant made a convincing showing of prejudice).

D. *Relevant Market*

Phonetele asserts as its final ground for reversal that the district court erred in limiting the relevant market to "ancillary stand-alone programmable toll restriction equipment electrically connected to the telephone network." *Excerpt of Record* 59. The definition of the relevant market is a factual inquiry reversible only for clear error. *Oltz v. St. Peter's Community Hosp.*, 861 F.2d 1440, 1446 (9th Cir. 1988). We find no clear error in the district court's market definition. The district court applied the correct legal standard in defining the market, limiting the market to include only products which could compete with the Phonemaster, as opposed to including all ancillary equipment whatever its function. *See United States v. E.I. duPont de Nemours & Co.*, 351 U.S. 377, 395 (1956). Phonetele does not inform us what it believes the proper market definition should be, arguing only that "the market must be defined as broadly as possible." Appellant's Brief at 60. Nor has Phonetele suggested how a change in the relevant market would affect the outcome of this case under any of its antitrust theories.

CONCLUSION

After the district court entered its decision in favor of AT&T, Phonetele was left with the impression that "something is seriously wrong with the opinion" of the district court. Appellant's Reply Brief at 24. Phonetele has not, however, succeeded in articulating to this court any reasons for this impression which would require remand or reversal. The district court's findings of fact are not clearly erroneous.

Phonetele was not prejudiced by the district court's delay in entering its decision. The judgment of the district court is AFFIRMED.

APPENDIX B

FILED
JUL 14 1988
Clerk U.S. District Court
Central District of California
By Deputy

UNITED STATES DISTICT COURT

CENTRAL DISTRICT OF CALIFORNIA

PHONETELE, INC., Plaintiff, vs. AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al., Defendants.	) CV74-3566-HLH)) FINDINGS OF FACT, CONCLUSIONS OF LAW, AND MEMORANDUM OPINION

The Court finds and concludes as follows:

1. Introduction: The plaintiff in this action is Phonetele, Inc. The defendants are American Telephone and Telegraph Company (hereinafter AT&T), Western Electric Company, Bell Telephone Laboratories, Incorporated (hereinafter Bell Labs), and Pacific Telephone and Telegraph

Company (hereinafter PT&T).[1] The essential claims presented in the action are that the defendants used their monopoly power over the telephone network to exclude from the market, or hinder free marketing of, the plaintiff's ancillary telephone device, called a Phonemaster. The antitrust issues are stated in several different ways. It is alleged that the requirement of a protective connecting arrangement (hereinafter PCA) was an anti-competitive device used to exclude or hinder the marketing of the Phonemaster, that the requirement that devices such as the Phonemaster be connected through a telephone company provided PCA was a tie-in arrangement, and that lack of availability of suitable PCAs was a device to hinder the marketing of the Phonemaster. It is also contended that, even when the PCA requirement was lifted, the defendants

further abused their monopoly power by refusing in various ways to properly market the Phonemaster while purporting to do so. A pendent claim is also alleged. It is alleged that the same activity which forms the basis of the antitrust claims was an intentional interference with prospective business advantage. The defendants (who may sometimes be referred to collectively as the Bell System) deny each of the allegations. They justify the requirement of the protective connecting arrangement as a necessary measure to protect the telephone system from possible harms coming about from the electrical interconnection of equipment not provided by the Bell System.

2. Summary history of the action: This action was filed in 1974. It was dismissed by the District Court[2] in 1977 on the basis that the Federal Communications Act (FCA) and the regulatory system

provided by the Act gave an implied immunity to the defendants by reason of the control of the Federal Communications Commission (hereinafter FCC) over the terms and conditions of "interconnection" of non-Bell System attachments to the telephone system. The dismissal of this action which ensued was appealed to the Ninth Circuit Court of Appeals. In Phonetele, Inc. v. American Tel. & Tel. Co. (9th Cir. 1981) 664 F.2d 716, The Court of Appeals reversed. The opinion of the Court of Appeals has governed the course of this case since. The opinion exhaustively and thoroughly analyzes the interaction of the antitrust laws and the FCA and provides standards for the determination of this case. The principal task of this Court is to apply to the facts learned during trial the standards provided by the Court of Appeals for decision of this case. This Court will not attempt to

repeat everything said in the opinion of the Court of Appeals, and a reading of that opinion is necessary for a full understanding of the background of this case. The matter has now been tried and is decided in these Findings, Conclusions, and Memorandum. Decision of the case has been delayed far longer than desirable by reason of the necessity to master the extensive factual record submitted.

3. National regulation up to the Carterfone decision: The telephone industry, a large proportion of which was controlled nationwide by the Bell System (until 1984), is heavily regulated and has been since the early 1900's by various state regulatory commissions (in California, the Public Utilities Commission, hereinafter CPUC). Since 1934 (the date of the FCA),[3] interstate telephone business has been regulated by the FCC. From the earliest

dats, the state regulators have required that the Bell System take complete responsibility for the operation of the telephone system. As a part of this requirement, telephone companies were required to own and operate all of the equipment necessary to the operation of the telephone system, to and including the telephone set in the hands of the user. The regulatory commissions took on the job of prescribing rates, to the end that telephone service would be available to the consumer on a basis of fair charges. These charges in effect were calculated to provide a fair but not excessive return to the telephone companies on their investments. This function of state regulation continues to this day. The Bell System did not resist the requirement that it own and furnish all of the equipment; in this sense it may be said that the state regulators and the Bell System saw

"eye-to-eye" with the necessity then seen by both as necessary to provide responsibility in the Bell Company for efficient and economical operation, and to provide the ability to the Bell System to meet that mandate. Thus, provision of telephone service, including ownership of all parts of the system between the calling telephone and the receiving telephone, became a monopoly of the local telephone companies. AT&T was the owner of a majority of the large local telephone companies, often called Bell Operating Companies (hereinafter BOCs). The parent company also owned the manufacturing and research units which serviced the BOCs. These were, respectively, Western Electric Company and Bell Labs. Bell Labs gained a reputation as a successful research and development arm of the telephone industry, developing the design for new equipment. Western Electric Company

manufactured substantially all of the equipment used in the Bell System. Formation of the FCC in 1934 did not immediately change this arrangement. FCC assumed the duty of regulating interstate telephone service provided by AT&T, both from the standpoint or rates and other methods of operation. FCC did this with a system of tariffs, required to be filed by AT&T much as the local BOCs were required to file tariffs with the local regulatory agencies. The tariffs prescribed not only rates, but other terms under which the telephone company's system was to be used by its customers. The tariffs historically prohibited any "foreign attachments" to the telephone network. This requirement, contained in the tariffs of AT&T and each of the BOCs, was required as a part of the longstanding historical concept that end to end responsibility for the operation of the telephone system could not be fixed on the telephone company

without also providing it full control and ownership of the parts that made up the telephone network. Thus the legal monopoly maintained by AT&T and the BOCs went not only to the ownership of the wires and switching operations which connected the telephones, but also the telephones and other terminal devices themselves. This sanctioned monopoly suffered its first crack in 1947 with the recording devices case before the FCC.[4] In that decision, the FCC allowed the attachment of devices to record telephone calls provided that a telephone company provided protective device be used with the recording system. The next crack in the foreign attachments tariff came with the Hush-A-Phone case in 1957.[5] Hush-A Phone involved merely a plastic mouthpiece which snapped over the speaker of the phone to provide privacy to the speaker. No electrical connection was involved. FCC ordered AT&T to allow its use. Thus, the stage was set for the beginning of

the revolution in the telephone business which commenced with the Carterfone decision in 1968[6] and culminated with the split-up of the Bell System effective January 1, 1984.[7] This case involves a small piece of that revolution.

The Carterfone was a device not electrically connected to the telephone system which allowed the telephone system to be connected to a private radio system. The voice communications transmitted over the telephone lines were, by acoustic and inductive techniques, able to be broadcast over a private radio system with the use of the Carterfone. No electrical connection was necessary, so that the imparting of electrical signals into the telephone lines was not accomplished by the Carterfone device separately from the equipment owned and provided by the telephone company. The exact meaning of the Carterfone opinion,

and the two opinions which immediately followed it on motion for reconsideration and establishment of a study on interconnection[8] is still the subject of dispute. However, the revolutionary nature of the Carterfone opinion to the telephone industry is shown by a short quotation from the opinion:

> "...A customer desiring to use an interconnecting device to improve the utility to him of both the telephone system and a private radio system should be able to do so, so long as the interconnection does not adversely affect the telephone company's operation or the telephone system's utility for others. ...We are not holding that the telephone companies may not prevent the use of devices which actually cause harm, or that they may not set up reasonable standards to be met by interconnection devices."

Thus, the telephone company was required to file new tariffs modifying the absolute prohibition against "foreign attachments."

The opinion of the Court of Appeals sets out in more detail just what Carterfone

held and did not hold. The defendants here challenge the accuracy of certain of the conclusions made by the Court of Appeals as to the affect and nature of the Carterfone opinion. However, this Court is bound by those conclusions and will follow them. In following the holding of the Court of Appeals as to the meaning of Carterfone, however, it must be recognized that the Court of Appeals did not, and did not purport to, follow all of the intermediate steps between the Carterfone opinion in 1968, and the ultimate orders of the FCC effective in 1976 prescribing a system of registration for ancillary and terminal equipment.[9] The fact that the Court of Appeals omitted certain of the intermediate steps taking place in the FCC does not mean that they are to be ignored. It simply means that to reach its decision the Court of Appeals did not need to follow in detail

the intricate path between Carterfone and registration. To the extent intermediate steps affect the application of the standards or tests prescribed for application in this case by the Court of Appeals, the Court believes it is free to look at those intermediate steps to determine the regulatory context in which AT&T acted in this period. However, to the extent that AT&T's argument would ask the Court to diverge from the interpretations of Carterfone reached by the Court of Appeals, this Court cannot do so. Thus, the regulatory steps involved between 1968 and 1976 may be examined to determine the regulatory context, but may not be used to impeach the statement by the Court of Appeals as to the meaning of Carterfone. At this point, before discussing the tests to be applied, the Court will turn to a description of the plaintiff's product and its place in the

market.

4. The Phonemaster: Carterfone started the deluge. Following Carterfone, it became apparent that many opportunities existed to provide specialized equipment to the telephone consumer either not provided by the Bell System, or less expensive than that offered by the Bell System. Entrepreneurs swarmed into the marketplace. Types of equipment involved ranged from the most sophisticated connections for modern computers to the most flimsy foreign made devices designed to be sold merely on the basis of price, not quality. How the Bell System coped with this will be set forth at a later place in this memorandum. One of the entrepreneurs coming into the marketplace was Phonetele, Inc. Phonetele developed a device called a call restrictor, named the "Phonemaster." The Phonemaster is a stand-alone, solid state computer which is designed to

require a telephone user to use the most economical path available in placing telephone calls, and to prevent unauthorized phone calls beyond the local calling area. The device used "solid-state" equipment, thus improving on the electro-mechanical systems of restriction devices then in use and tariffed by many of the BOCs. The Phonemaster was designed to be inserted in the telephone line behind (that is, on the central telephone office side) of a PBX, and in some situations, a key telephone system. The marketing appeal of the Phonemaster is basically to a medium or large sized business organization which has numerous telephone extensions used by employees or other persons present at the business (customers of a hotel, patients of a hospital, etc.). The purpose of the Phonemaster is to allow the business proprietor to limit the types of calls which

may be made from any particular telephone extension. Thus, employees, hotel customers, hospital patients, etc., can be limited to local calls or calls otherwise permitted by the business proprietor. The Phonemaster is "programmable," meaning that necessary adjustments can be made to allow some out-of-zone or area calls, but not others. For example, a business proprietor may allow his salesman to call into a particular long distance area, or another message unit area, but exclude other calls which are not authorized by the business proprietor. The Phonemaster as it ultimately developed could be reprogrammed when the needs of the businesses changed by the substitution of a new "chip" which could be plugged into the proper position in the circuit boards in the interstices of the machine. The Phonemaster was also flexible enough to allow certain "levels" of service. This means

that certain groups of executives within a business organization would be allowed greater freedom to make uncontrolled calls than used by other operations which did not need such freedom. The Phonemaster allowed seven-digit programming, a significant advance over other models on the market. Thus, a particular phone user could be allowed to dial a particular prefix in another area code, but not other prefixes in other area codes (for example, a Los Angeles user in area code 213 could be allowed to dial the 1, a New York area code (212), and a particular three-digit prefix in that area code, without allowing wider calling privileges).

In addition, the Phonemaster could be programmed to require the telephone user to utilize certain Bell System provided options for reducing the costs of phone service. For example, the Bell System

provided in some areas flat rate direct service from one central office to another (called FX or foreign exchange service). The Phonemaster could be programmed to require a user to use the direct line rather than go through the more expensive routing available. Certain areas of the country used "zones" within area code designations. In Los Angeles, these involve the familiar "message unit" calls. Calls outside of an immediate dialing area, even within the area code, in areas where zoning was used, cost more than local calls. The Phonemaster could be programmed to allow calls into certain message unit areas but not others, or to require that calls to certain message unit areas be carried over telephone lines acquired at lesser price under special programs of the local BOC rather than be just dialed directly at greater cost.

The Phonemaster had as its greatest market a use behind electromechanical type PBXs. When the Phonemaster came on the market in the early 1970's, the predominant method of serving medium to large business was through a telephone company provided PBX rented to the subscribing business. At that time, the PBXs were largely of electro-mechanical design, although a shift was soon to start to solid-state PBXs which, among other features, had call restriction capability. The PBX was traditionally operated by a subscriber's employee. Typically, the Phonemaster came equipped with a "override switch," allowing the PBX operator to make exceptions to the restriction automatically provided by the Phonemaster, in accordance with the employer's policies.

When a telephone user in a facility serviced by the Phonemaster placed a call not permitted by the business proprietor,

the Phonemaster monitored the number dialed and, if not permitted under the programming, "opened the line" which effectively prevented the call from being further continued on the telephone lines. The Phonemaster then notified the telephone user that he had been "restricted" by playing back in the user's earphone a distinctive tune (the first four notes from Beethoven's Fifth Symphony). (This became a source of controversy with AT&T later; see below.) The Phonemaster, as a sophisticated device, had a significant cost. Therefore, it was economically to be used only in businesses with significant telephone traffic, where the costs to be saved by call restriction services exceeded the costs of the Phonemaster. For all practical purposes, this meant that the principal use of the Phonemaster was behind telephone systems large enough to employ a PBX. However, the Phonemaster

could be used in a key system network, which primarily was designed for fewer telephones. A small number of Phonemasters were ultimately sold to be used behind key systems, but usually only when a particular business proprietor felt that extensive misuse of the phone system was being made so that the cost was justified. This was a minor part of the Phonetele market.

The earlier models of the Phonemaster were usable only with dial telephones. After the Phonemaster had been on the market for a period of time, telephone usage more and more turned to "Touch-Tone" telephones, where the signals were audibly transmitted rather than transmitted by electrical impulses generated by the turning dial. By 1976, Phonemaster had been upgraded to a system which would handle both dial and Touch-Tone phones. Phonemaster was suitable from then on in businesses where the

telephones were being converted to Touch-Tone telephones. In addition, as the latter half of the 1970's appraoched, both the Bell System and outside manufacturers came into the market with modern solid-state PBXs. These PBXs were of many varieties, but the more advanced ones of them had call restriction capability built into them. Where the business converted to a modern solid state PBX, whether of Bell System or other origin, the Phonemaster became obsolete. However, older model electro-mechanical PBXs still could use the Phonemaster as an adjunct to it.

Market conditions suitable to the Phonemaster also varied throughout the country. The zone or message unit system familiar in the Los Angeles and certain other large metropolitan areas is not a nationwide system. Many areas of the country had a "flat rate" for all local calls.

Others had a flat rate for local calls within an extensive area. In such areas, the Phonemaster was relatively less economic, since the bulk of business telephone service could not achieve the necessary savings to pay for the expensive cost of Phonemaster equipment. The Phonemaster was most economically used in areas such as Los Angeles and San Francisco, where there was multiple zoning throughout a large urban area, or San Francisco, where there were multiple area codes throughout a large urban area.

Phonetele started in late 1970, and had its first products ready for distribution in 1971. It thus entered the ancillary telephone equipment business after the Carterfone tariffs had gone into effect but while the final shape or end of the massive change in the telephone business was yet to be determined.

By and large, the Phonemaster was designed and manufactured with proper engineering standards and competently. There were certain technical problems with the Phonemaster which had to be corrected from time to time. Each time the technical problems arose, they were diagnosed and solved in due course by Phonetele. Thus, Phonemaster had a transformer unit which failed from time to time amidst emissions of smoke. The problem turned out to be a faulty transformer, not designed to Underwriting Laboratory standards. When diagnosed, the problem was corrected by Phonetele. Phonemaster also had a tendency to impart "longitudinal imbalance" into the telephone lines. Whether this is a "harm" to the telephone system was a matter of degree; the Phonemaster's deviation from telephone company standards was small, but present. This was a correctable defect but, according

to the evidence, not corrected until 1974, when the Phonemaster was tariffed by PT&T. There were other problems that occurred from time to time. These defects, and others, do not appear to be, and are found not to be more numerous or significant than in any other type of sophisticated equipment. There were other features to be discussed below, which caused disagreement between Phonetele and the Bell System, more related to legal considerations regarding division of responsibility than to actual operation in the field. In summary, the Phonemaster was a valuable product in the situation where its services were needed.

5. "Relevant Market": Any monopoly case depends upon the definition of "relevant market." In this case, identification of the "relevant market" has taken a relatively low priority by reason of the principal issue affecting the PCA.

Nevertheless, "relevant market" should be defined for purposes of this case. The Court finds that the relevant market is ancillary stand-alone programmable toll restriction equipment electrically connected to the telephone network. Several other possible definitions of the relevant market are rejected. Plaintiff suggests that the relevant market is ancillary telephone equipment. The Court rejects this suggestion as far too broad. While other ancillary equipment electrically connected to the telephone network did have the protective connecting arrangement problems in common with toll restrictors, such equipment was so varied, and the problems of connecting to the network so diverse, that one cannot be compared to the other. The usual definition of "relevant market" involves competing products.[10] The products most closely competing with the Phonemaster were other

stand alone toll restrictors. In addition, the "relevant market" should be defined to include use of the stand alone toll restrictors behind non-programmable electromechanical PBXs without sophisticated toll restriction capability. In this market, the Bell System did not compete (except marginally for a period of time with the Call Controller). The primary competitors were Stromberg-Carlson (until about 1977 or 1978), North Electric, and Mitel. The Call Controller was a marginal competitor from 1974 to 1977 in the portion of the relevant market which involved small limited capacity PBXs.

The definition of "relevant market" does not include modern solid state PBXs which had as one of many features programmable toll restriction. The reason is that such PBXs served many other purposes than toll restriction, which was a minor part of

the features of such PBXs. The Court concludes that such modern solid state PBXs do not compete in the relevant market, although they do make obsolete the market for programmable stand alone call restriction electrically connected equipment. Toll restriction equipment is not designed to compete with a PBX; instead, it is used to amplify the range of utility of a certain type of PBX. Accordingly, the Court does not view modern PBX solid-state equipment as a part of the relevant market.

6. Post-Carterfone tariffs and their aftermath: It is now time to return to the regulatory context in which Phonetele entered business in late 1970 or in 1971. Carterfone was decided in 1968. The foreign attachment tariff, prohibiting all foreign attachments, was struck down and AT&T was invited to file new tariffs. At the time, AT&T construed the Carterfone decision to

apply only to non-electrically connected attachments and not to allow substitutions of equipment in the existing telephone network. As to the first part, non-electrical attachments, we now know from the Court of Appeals opinion that Carterfone was not so limited, and applied to any attachments to the phone company, whether electrically connected or not. As to the second part, however, the telephone company was correct, as the FCC expressly said in its order denying reconsideration[11] of the Carterfone decision:

> "The facts of this case did not involve the furnishing of purely telephone system equipment telephone-to-telephone on the message toll telephone system."

And, in its first opinion on the new post-Carterfone tariffs, the Commission again expressly said:[12]

> "Our decision in Carterfone does not hold that a customer may substitute his own equipment or

> facilities (whether it be telephone instruments, loops, poles, or central office equipments) for that furnished by the telephone company in providing message toll service as that service is defined in the tariff. Our decision dealt with interconnections and not replacements of any part of the telephone system."

Nevertheless, the dispute about what Carterfone did and did not do still rages, as is evident from the detailed discussion in the opinion of the Court of Appeals. The telephone company decided to go beyond what it conceived to be the requirements of the Carterfone decision.[13] First, the new tariff allowed electrically connected equipment of other manufacturers to be attached to the telephone system. Secondly, it allowed substitutions of terminal equipment in the telephone network. However, permission to attach electrical equipment, whether of the ancillary or the terminal type, was conditioned upon attachment through a

"connecting arrangement," supplied by the Bell System. The new tariffs were the subject of immediate and intense attack in the FCC. The FCC determined several things in its 1968 order[14] allowing the tariffs to go into effect. First, the Commission expressly decided that the new tariffs did not violate Carterfone.[15] Secondly, the Commission determined that it would not "approve" the tariffs. The Commission reasoned that allowing widespread connection of attachments to the telephone system, electrical or not, was a revolutionary change in the telephone industry as it had been known up to that date. It acknowledged that the effect of such attachments or substitutions of equipment in the telephone system provided both technical problems and potential financial problems of wide range and affect. The Commission determined that it wanted to study the effect of interconnection with

electrical attachments to the network before it proceeded to any further stages. The effect of allowing the tariffs to go into effect without "approval" was to reserve jurisdiction to make further orders following the results of study over a period of time.

The Commission implemented a study period, which lasted until 1976, on both an economic and technical level. The studies ended in 1976 with the requirement that a registration program be created, that all electrical attachments and terminal equipment had to meet certain registration standards fixed by the Commission, that cerfification of meeting those standards had to be filed before a non-Bell System manufactured electrical device could be inserted into the telephone system, and required that any non-certified device be connected through a PCA. The eight years from

Carterfone (1968) to registration (1976) provide the principal focus of the controversy in this case. Plaintiff contends that the Bell System should have instituted a registration program immediately after Carterfone and that AT&T's failure to do so was caused by anti-competitive attempts to delay, hinder and prevent it and other manufacturers from entering the telephone equipment market. The Bell System contends that its actions during this period of time were motivated solely by a desire to provide physical protection to the network and in recognition of the monetary requirements of the regulatory system as it then existed. These contentions frame the issues to be decided.

7. The Court of Appeals tests to be applied: In rejecting the defendants' contention that an implied immunity existed for the post-Carterfone tariffs containing

the PCA requirement, the Court of Appeals held that the antitrust laws (particularly, here, the anti-monopoly provisions of Section 2 of the Sherman Act) were applicable to the defendants despite the regulatory context in which they operated. However the Court of Appeals indicated that the imperatives of the regulatory system are to be considered in determining whether actions of the defendants were "reasonable." The language used by the Court of Appeals should be quoted at this point, since it will provide the major basis of further discussion of the problem. After holding that there is no immunity, and that the filing of a tariff itself does not bring immunity, the Court of Appeals said at pages 737-38 as follows:

> "When the regulated entity assertedly attempts to respond to its duties as a common carrier by filing and implementing an anti-competitive tariff, the antitrust laws do not apply to the tariff without regard to the

technical and legal constraints flowing from the regulatory structure. If a defendant can establish that, at the time the various anti-competitive acts alleged here were taken, it had a reasonable basis to conclude that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority, then its actions did not violate the antitrust laws. At this stage of the proceedings, it appears this inquiry will depend largely on whether the facts show the companies did reasonably conclude, given their expertise, that uncontrolled NCSU interconnections would endanger their own equipment or disrupt their own single transmissions in identifiable ways, and also that the tariff as filed was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such real harm from occurring. These matters must be developed as trial."

The Court of Appeals also stated what was not to be considered (at page 738):

"The defendants may not justify their actions based on some mistake of law in interpreting the FCA or judicial or FCC decisions. It will not be open to a defendant to argue that it was entitled as a matter of right to file any

> tariff it chose or that it was obligated to file a tariff absent the kind of factual necessities we have outlined above. After the Carterfone decision, a defendant may not assert that it was entitled by law or agency policy to a monopoly in the furnishings and supply of terminal equipment."

Thus, this Court has its marching orders. It has been told what it must consider and what it may not consider. The prohibition on interconnection of "foreign attachments" is an antitrust violation in this monopoly setting unless the defendant can justify the restriction under the standards quoted. It is apparent that the defendant has the burden of proof. It is also apparent that the tests to be applied are both subjective and objective. The tests are objective in the sense that the PCA requirement must be a "reasonable, properly focused mechanism, considering other alternatives than available, to prevent such real harm from occurring." In addition, the defendants had

to "reasonably" conclude, given their expertise, that connections without the PCA were dangerous to telephone company equipment or interfered with signal transmissions "in identifiable ways." The opinion goes on to make clear that the tests set forth above are applicable to the tying claims, the claims of violation of Section 2 of the Sherman Act, and any claims which may be made involving violations of Section 1 of the Sherman Act, insofar as they are based upon tariff requirements that a PCA be used to connect electrical equipment to the telephone system.

The Court of Appeals does not expressly answer a question made relevant by the course of evidence in this case. The problem is posed by the fact that the defendants approached the problem of interconnection, and the filing of the Carterfone tariffs, from the standpoint of dangers to

the system from the interconnection of unknown multitudes of electrical equipment. The plaintiff, on the other hand, insists that its particular equipment posed no danger to the system and demands that its device be considered alone under the standards set forth by the Court of Appeals. The question posed therefore is whether the tests to be applied are from the dangers presented by an amorphous mass of electrically connected ancillary telephone devices, or whether the tests are to be applied device by device. Neither the Court of Appeals opinion nor post-Carterfone decisions of the FCC expressly answer this question. It is the Court's opinion that what must be considered is whether ancillary equipment of a particular type poses dangers to the telephone system under the Court of Appeals standards, and not whether a particular manufactured device necessarily

poses such dangers. Accordingly, the inquiry must be whether telephone call restriction equipment in general poses the types of dangers that were outlined in the Court of Appeals opinion, and not specifically only whether the Phonemaster provides such dangers. The Court comes to this conclusion for a number of reasons. First, the legal constraints on the telephone company is that their tariffs apply equally to all; the tariffs may not make separate rules for one device than they make for another. Second, when examined from the standpoint of the reasonableness of the post-Carterfone tariffs, the question is a broad one: What is necessary in general to protect the phone network from the consequences of uncontrolled electrical interconnection? Thus, the reasonableness of the Carterfone tariffs must be judged from the standpoint of the mass of electrically connected devices to be

considered, not from the standpoint of whether the Phonemaster (non-existent at that time) has particular circuitry which will protect the system.

Another aspect of the Court of Appeals opinion is adverted to above. It is noted that the Court of Appeals attributes to the Carterfone decision, and not voluntary AT&T action in filing the post-Carterfone tariffs the "credit" for allowing terminal equipment to be connected to the telephone system. If it makes a difference, the Court is bound by the interpretation of the Court of Appeals even if convinced by the express language of the FCC opinions to the contrary. However the Court has determined that nothing in this case depends upon straightening out this part of the historical record.

8. From Carterfone tariffs to registration: In filing the Carterfone tariffs, the telephone company acted under

time pressures. The FCC had struck down the previous foreign attachment prohibitions. The question immediately presented on a time limited basis was what should replace them. Non-electrically connected devices presented the telephone company no problem; they had to and did permit them subject only to prohibition if there was actual harm to the network. No connective devices or registration was required as to such non-electrically connected attachments. The principal immediate problem faced by the Bell System was to prevent technical harm to the telephone network from electrical attachments. As plaintiff indicated at final argument (while criticizing the phone company for its failure to develop a registration or standards program prior to Carterfone), a PCA requirement for a short period of time at least was not unreasonable. Plaintiff's attack during the case was

based upon the alleged failure of AT&T to develop a standards or registration program in the period following the filing of the Carterfone tariff. Plaintiff attributes this to pure unadulterated anti-competitive intention and affect. The Court finds to the contrary.

The engineers of the Bell System were greatly concerned about the quality of the new attachments to their system. They knew that the components to be attached to the system were to be manufactured anywhere by anybody, technically qualified or not, and motivated to provide high quality or not. They knew, as is the fact, that a certain number of manufacturers of electrical equipment to be attached to the telephone system would have no interest in the long lasting quality of the system, but an interest only in the monetary rewards to be seen by the manufacture of inexpensive low quality

devices for a certain segment of the market. The engineers also knew, and were proud of, the technical accomplishments of the American telephone system in providing what they proclaimed was "the finest telephone system in the world" with high standards of equipment, design, maintenance, and installation. They did not want that system to be degraded, as they saw from a comparison with telephone systems in other parts of the world, by allowing the attachment of law quality equipment which, over time, was feared to degrade the system. The Court finds that this pride and motivation in quality service was a significant factor in many of the Bell Company decisions in this era, and had nothing to do with anti-competitive intentions. As the post-Carterfone tariffs were filed, there were two obvious means of protecting the network from harm or degradation by electrically attached ancillary or

or terminal equipment. The first method was by the connection of such equipment through a protective connecting arrangement (PCA). The second was through development of a set of standards which would be required to be met by the "foreign attachment" before it could be connected to the network. The standards approach had a number of problems within it. Some of those problems were:

a. Who devises the standards?

b. Who approves a particular piece of equipment as meeting the standards?

c. Should the "foreign attachment" be inspected to see if it meets the represented standards, and if so, who should do it?

d. Should installation be required to be done by a trained person, and if so, who provides that person and supervises the installation?

e. Should the equipment be maintained, and if so, who does it?

As the Carterfone tariffs were filed, neither AT&T, the manufacturers of the ancillary and terminal equipment, nor the FCC had answers to the questions involving the registration or standards approach. The Court concludes that, at the time of the filing of the post-Carterfone tariffs, the facts show that the defendant companies did reasonably conclude, given their expertise, that uncontrolled NCSU interconnection would endanger their own equipment or disrupt their signal transmission in identifiable ways. It also concludes that the tariff as filed was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such harm from occurring. Thus, the post-Carterfone tariffs, requiring as they did a PCA, were justified.

This only begins the inquiry, however, and does not end it. The plaintiff's major contention is that subsequent action by AT&T in failing to implement a standards program was, nevertheless, in violation of the tests specified by the Court of Appeals.

It is necessary, therefore, to follow the course of the post-Carterfone proceedings from 1968, when the tariffs were filed, to 1976, when registration was imposed by the FCC.

It will be recalled that the FCC, in allowing the filing of the Carterfone tariffs (without specific approval of them) stated its intention to study the effects of interconnection, both technically and economically. The first step taken by the FCC in this effect was to obtain technical advice. The National Academy of Sciences (hereinafter NAS) was requested to review the technical problems of the electrical

connection of non-Bell System devices to the network. A prestigious panel was assembled. The panel made a comprehensive study of the technical problems and how harm might be prevented when non-Bell System equipment was attached. The report of the NAS panel was rendered to the FCC in June, 1970. The NAS report did not deal with political, policy, or financial considerations of interconnection. It confined its study strictly to potential harm to the network and realistic methods of preventing such harm. It examined both the PCA and registration possibilities. The panel identified the general categories of harm which could be imparted into the network by the electrical connection of ancillary and terminal devices. These harms were, generically, fourfold: (1) voltages dangerous to human life, (2) signals of excessive amplitude, (3) improper line

balance, and (4) improper control signals.

The telephone system works on substantially less voltage than the commonly used potentially injurious 110 voltage found in operating most household appliances. Most devices electrically connected to the telephone system use 110 voltage to power them (including the Phonemaster). With direct electrical connection, it is necessary to protect the telephone lines from the accidental entry of 110 voltage. Thus, either the device must be properly designed to prevent the entry of 110 voltage into the telephone lines under any foreseeable circumstance, or the telephone company must take its own steps to prevent such entry.

Telephone signals of excessive strength do harm to the network because they interfere with the use of the network by other customers. Excessive strength signals "leak" into neighboring telephone

lines causing noise and "cross talk" on other lines. Accordingly, the strength of the signal carrying the voice imparted into the telephone lines must be contained within the limits necessary to be heard at the other end, but not so high as to interfere with other conversations in the network.

Improper line balance results from the introduction of a higher current to one side of the line than the other. When this happens, cross talk or other interference with other lines takes place. Accordingly, the current carried by the two sides of the line must be within certain parameters to prevent degradation of service on other lines.

Improper control signals can cause a myriad of effects, including misdirecting of the call from its intended destination. Telephone company central offices provide switching mechanisms directed by the

electric impulses imparted into the line. These impulses operate the switching system which directs the call to its intended destination. The signals also perform a number of other functions, including the recording of the call for billing purposes, the return signals (i.e., busy, dial tone, simulation of ringing, etc.) into the system familiar to the telephone user.

To meet these technical requirements, control (achieved by the use of such devices as transformers and capacitors) of the electrical signals emanating from the attachment of terminal equipment must be maintained. The maintenance of such control is the principal reason why the telephone company had insisted over the years that it have end to end control over the telephone equipment. With the elimination of that concept, other mechanisms needed to be devised to provide such control.

The NAS study examined how these controls could be maintained with free interconnection of the devices of manufacturers other than the Bell System. The study concluded that the PCA was one technically acceptable way to provide the necessary controls. The protective connecting arrangement in this contemplation would provide the necessary transformers, capacitors, relays, fuses, etc. to regulate the input into the telephone company lines so that a failure or misdesign on the part of the terminal or attachment would not affect the quality of telephone services to others, even though it might affect such quality to the owner of the equipment.

The panel also reported on the feasibility of a registration and certification system using standards. The report stated:

> "The Panel emphasizes that the development of standards in a program of certification requires

> a complete system of control, which will not be effective unless all elements of the system, as described in this report, are adopted. For example, the development of standards alone is inadequate. Certification of equipment without certification of installation, testing, and maintenance will be ineffective in protecting personnel, facilities, services, etc."

It is apparent that there were registration programs and registration programs. The NAS study recommended a registration-certification program only if four steps were a part of such a program: (1) approval of the design, (2) certification of installation methods, (3) testing of the equipment, and (4) maintenance steps.

Having received this report, the FCC proceeded to the next step. They commissioned the so-called Dittberner Report. The Dittberner Report was a consultant's study designed to evaluate the practical methods by which the recommendations of the NAS

panel could be implemented. The Dittberner Report was not a technical study of the harms, but commented on the realism of the methods proposed to control them. The Dittberner Report was critical of the time, expense, and effort necessary to implement the registration-certification approach as recommended. It was indicated, probably correctly, that a large government bureaucracy would have to be created to write the standards, supervise the installation and testing, and make sure the seller followed up on maintenance. The Dittberner Report was, therefore, discouraging of the realistic possibility that a registration-certification approach as recommended by the NAS be implemented.

The FCC established several study committees in the ensuing period to study the possibility of a standards approach with regard to certain pieces of equipment.

Because the most important piece of equipment involved was the PBX, a PBX study committee was formed in 1971. AT&T provided members of this committee, and as did others. The purpose of this committee was to attempt to develop a standards program for PBXs. AT&T participated fully in the work of this committee. Plaintiff criticizes AT&T's participation as merely an attempt to give a false impression that AT&T was willing to study certification, and as further an attempt to slow down or "drag its heels" on producing a realistic committee report. Nothing supports this charge, and the Court rejects it.

Another committee was formed in 1972 to study the use of standards for automatic dialers and answering equipment. Such standards were developed and went into effect in the interim period.

Phonetele requested the FCC to create a committee specifically to study the question of a standards program for call restrictors. The FCC declined, however, to do so. The CPUC did conduct such a study in 1973, but after a set of standards were developed, the CPUC declined to create a certification program specifically for call restrictors. In 1975, the CPUC did establish a broader certification program applicable to all data and ancillary devices, similar to the program adopted that same year by the FCC. It is plaintiff's contention that AT&T acted unreasonably in not establishing a certification program for call restrictors, or not requesting the FCC to do so. The Court rejects this contention. FCC was proceeding to study the complex requirements of a registration certification program, and to master the various options and intricacies in such a program, on a

step-by-step basis. This approach had been recommended by the NAS in its report, which recommended that the FCC begin its study with the PBX. While Phonetele would have liked priority for its product, the careful study implemented by the FCC, with which AT&T cooperated, was necessary for the development of a standards program which was technically protective of the network, financially feasible, and in the interest of orderly change in basic industry understandings then taking place.

By approximately 1972, it became apparent that financial considerations needed to be considered in the development of any revolutionary policy. The reason was as follows:

Revenue of the telephone company was divided between the long distance operation, run by AT&T, and the local telephone companies, in accordance with certain formulas.

Historically, over the years, local BOCs had been under heavy pressure from state regulatory agencies to make telephone service to individual homeowners available at low cost. In addition, over the years, local regulatory agencies had placed pressure on the BOCs to shift as much of the overhead as feasible to business equipment, to the end that residential equipment would receive lower rates. Rate structures accomplishing what the local regulatory agencies insisted on became embedded in the Bell System as a whole. The result was, in general, that local residential telephone service was "subsidized" by long distance service and business service. The effect of unrestricted interconnection of business-type devices (and the unrelated but concurrent development of competition in the long distance telephone business) threatened continuance of these cross-subsidies. Obviously, if

AT&T and BOCs had to compete with non-Bell suppliers of PBXs, key systems, and ancillary telephone equipment, they had to compete on the basis of price. That being the case, charges necessary to support a subsidy of home telephone service could not be continued. This problem became apparent to state regulatory commissions as a part of the problem related to interconnection of non-Bell devices. The state regulatory commissions protested in strong terms to the FCC. AT&T also brought to the attention of the FCC the potential affect on the rate structure of unrestricted interconnection. FCC had declined to consider this affect in its Carterfone decision. However, in 1974, FCC initiated a study separate from the technical study on the effects of interconnection on the rate structure. In addition, the state regulators, most concerned with this problem, instituted (through

NARUC) their own inquiry into the economic consequences of allowing interconnection of non-Bell equipment. NARUC found that widespread substitution of non-Bell equipment would necessarily cause an increase in the rates for local service. The state regulators, with exceptions, vigorously opposed the certification-registration system, and certain state regulatory agencies would not adopt the post-Carterfone tariffs allowing the substitution of non-Bell equipment. Bell contended then (and believes to this day) that the "unbundling" of telephone charges inherent in a system which allows free substitutions to the network will cause a significant rise in local revenue rates as a consequence of decreasing revenue from long distance service and provision of business-type telephone equipment.

The Court of Appeals opinion does not give guidance as to how to approach

this problem. HOwever, it is apparent from the subsequent course of FCC proceedings, that the FCC itself reached its final decision on interconnection policy without significant consideration of the financial effect of interconnection,[16] In essence, that decision was made in 1968 with the Carterfone tariffs. While the effect of the Carterfone decision on the economics was and continues to be a part of the revolution in the telephone business, it plays a small part in this case. Because the FCC paid little or no attention to the effect of unbundling of telephone charges, it cannot be said, in the words of the Court of Appeals, that this was a "factual imperative recognized as legitimate by the regulatory authority." However, in another sense, the pressure placed on the Bell System by the local regulators may be considered because this involvement was considered by the FCC.

In April 1974, the FCC created a new proceeding (Docket 20003) to investigate the economic consequences of interconnection. However, the registration-certification program was implemented before conclusion of that study. In addition, the FCC took vigorous action to prevent state regulatory commissions from themselves prohibiting substitutions of terminal equipment. In Telerent Leasing Corp. (1974) 45 FCC2d, 204, the FCC asserted its primacy (to the exclusion of state regulatory bodies) over the question of interconnection. Also in 1975, the FCC for the first time expressly approved the portion of the post-Carterfone tariffs which permitted substitutions as well as attachments.[17]

By 1972, it was apparent that the staff of the FCC was tending to favor a registration system without the requirement of certification of installation, testing,

or maintenance. This was primarily because of the lower cost of such programs, and not because another answer had been found to the concerns of the NAS panel. AT&T watched these developments with dire foreboding. While it was willing to consider a properly administered standards program along the lines recommended by the NAS panel, the Bell System did not feel that it itself could administer the program. No one else connected with the subject matter suggested that the Bell System administer the program, either. The reason is that the Bell System would be setting standards for its competitors, and supervising the manufacturing, installation, and maintenance of competitors equipment, or at least prescribing how it was to be done. The Bell System did not want to do that, the manufacturers did not want to have it done by the Bell System, and the FCC never seriously considered that

AT&T be required to do this. The alternative, however, was the creation of a government bureaucracy to administer such a program. Possible alternatives involved the creation of an independent agency (private or otherwise) set up under the aegis of the FCC to administer such a program. Because large sums of money and substantial bureaucracy were involved however it was handled, it became apparent that there was no enthusiasm or real push within the FCC to establish a certification-registration program such as recommended by NAS. In 1973, AT&T had to make a decision as to whether it would accept a registration-certification system without monitoring of installation, testing, and maintenance, or not. In short, acceptance meant that AT&T would need to accept a registration-certification system based upon paper approval of the plans submitted by the manufacturers without

follow-up to see that the device actually was constructed and worked in accordance with the plan. AT&T rebelled. The decision was made by its then chairman, John deButts. In a 1973 speech (referred to by the parties as "The Speech") to the association of state regulators (NARUC) Chairman deButts expressed and explained the opposition of AT&T to a registration program which did not have the four features listed above. Prior to the 1973 decision, AT&T had not taken a position on a registration program, although it had reservations about any program without the "four features." Thus, in default of any other solution to protect the network, AT&T decided to stick with its PCA requirement and to resist attempts within the FCC to impose a certification requirement without the "four features."

The decision to oppose certification was made in March, 1973, and announced to

the shareholders in April, 1973. AT&T's policy to oppose certification was described and defended in Mr. deButt's NARUC speech in September, 1973. Prior to the determination to oppose certification, AT&T was willing to accept a certification-registration program in the form originally opposed by the NAS panel. AT&T also took the position that it itself could not set the standards, do the inspecting and testing, and approve ancillary devices. It took this position for legal reasons; it believed it would be subject to antitrust and other claims by suppliers of material that AT&T disapproved. The Court concludes AT&T's position in this respect was reasonable. The position of AT&T not to favor a certification-registration program was a reasonable position in the sense that AT&T "did reasonably conclude, given their expertise, that uncontrolled NCSU

interconnectiom would endanger their own equipment or disrupt their own signal transmission in identifiable ways" and AT&T "had a reasonable basis to conclude that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority." In reaching this conclusion, the Court notes the following factors: First, that non-Bell System attachments and terminal equipment in general pose the risk of a substantial number of substandard parts and electrical circuitry that collectively posed a real danger of harm to the network unless controlled either by a PCA or by the four element certification-registration program proposed by NAS. Second, that for legal reasons, it could not on its own set the standards, inspect, approve or reject, supervise the installation of, and thereafter count on the maintenance of said equipment. Third, that while

many manufacturers would in good faith attempt, to the extent of their varying abilities, to meet the engineering standards required, in some case their abilities would not suffice to allow the equipment to meet the required standard, and in other cases manufacturers interested only in price competition would not attempt in good faith to meet the engineering, manufacturing, installation, and maintenance standards. Fourth, that the result is that a registration-certification program necessary in AT&T's judgment to accomplish the goals would have to be administered by a government agency or by a separately funded private agency under the supervision of the FCC. Next, the FCC had no intention or desire to institute the necessary four element certification-registration plan, and intended to rely only on a registration plan which required paperwork approval of

the plans for the various devices to be attached. AT&T reached these conclusions after long study and bonafide effort to devise registration-certification plans acceptable to it and in doing so worked diligently on FCC sponsored committees studying the same in the areas of particular equipment. The Court concludes that AT&T's concern about degradation of the phone system was reasonable, given its then knowledge and expertise. The Court rejects the argument of plaintiff that AT&T's positions during the "era of the PCA" was made for purposes of delay in order to permit the Bell System to be prepared to meet competition. The Court also rejects the plaintiff's argument that AT&T knew all during the "PCA era" that certification-registration was inevitable. The Court rejects the contention that the whole purpose of opposition to the registration requirement

was to monopolize for the benefit of AT&T and its subsidiaries the market in ancillary and terminal equipment, rather than a genuine interest in the quality of the network. In these respects, the Court notes the following: The period between Carterfone and the ultimate registration plan adopted by the FCC in 1976 was one of transition in the industry. Carterfone in 1968 marked the beginning of the revolution; the registration plan effective 1976 marked the end of it. During this period, it was clear to all in the industry that a major change was underway. The FCC had indicated its desire to study the method by which change should come about and had proceeded to do so on a number of levels. AT&T understood that change was upon it. The AT&T actions during the "PCA era" were consistent with this acceptance of the era of change, and its insistence that change take place in a way which would

maintain the quality of telephone service. A number of AT&T's actions illustrate this attitude. First, the decision of Mr. Romnes, immediately following Carterfone, was to go beyond the requirement of the Carterfone decision and allow substitution of terminal equipment to the network, provided that the same was done through a PCA. This marked an epic change in basic policy in the telephone industry (the policy of both AT&T and the regulators) that the telephone company was strictly responsible for "end to end service" and that that service had to be through Bell System property in order to allow the imposition of such responsibility. With the agreement to attach ancillary electrical powered equipment or to replace terminal equipment, subject to the PCA requirement, the telephone company took the lead in redefining the terms of its respons-bility. In the case where such equipment was

attached, the Bell System's responsibility was from PCA to PCA. Secondly, the Bell System assiduously studied and participated in the FCC studies of registration programs. In certain minor respects, the Bell System agreed to registration programs as to particular types of equipment. It did not oppose registration-certification formally until it became clear that it would not get a program which it thought was necessary to maintain the quality of the network. Lastly, it insisted that a study of the economic consequences be included along with the study of the registration-certification program. The FCC agreed to the extent that it established in 1974 a study on the economics of attachment and substitution. The FCC did not agree with AT&T and the state regulatory agencies, who in this respect joined with AT&T, that a resolution of the economic problems was necessary before

a full scale registration program went into effect. With regard to cost, AT&T initially believed that low cost simplified PCAs were possible. As time went on, it became clear that the engineering problems were such that a wide variety of PCAs needed to be manufactured to meet the different technical requirements of the varying ancillary and terminal equipment, and that the cost would be more than nominal. Nevertheless, AT&T reasonably believed, and the Court finds, that the cost of a registration-certification program meeting the four elements recommended by the NAS panel would also carry with it a substantial cost, probably exceeding the cost of the PCA program for which it would substitute. In addition, while PCA costs were not nominal, and therefore tended to increase the cost to the customer of using a non-Bell attachment or terminal equipment, nevertheless the cost

differential was not as much as the tariff cost of the PCA. The reason for this was that the transformers, capacitors, fuses, relays, etc., used in the PCA need not be duplicated by the manufacturer in the basic equipment, thereby reducing the difference in cost to a significantly lesser level than the tariffed cost of the PCA. In the respects set forth above, the Court accepts as credible the testimony of Charles H. Elmendorf, III, who had principal technical charge of AT&T's study during the PCA era.

Following the decision of AT&T to oppose a certification-registration program, AT&T expressed its position strongly before the FCC. The expression of this opposition in the FCC is protected by the doctrine of the Noerr[18] and Pennington[19] cases, which will be set forth below. However, Noerr-Pennington is not decisive, since factors other than expression of position in the

FCC, can lead to antitrust liability. To the extent that AT&T did express its opposition to certification from 1973 to 1976 in FCC proceedings, and carried that opposition into subsequent court review, the Court determines that said opposition was not a sham and was therefcre entitled to First Amendment protection. This is based on the determinations set forth.

The PCA era came to an end in 1976 with the effectiveness of a registration program prescribed by the FCC. This determination was set forth in two decisions of the FCC.[20] In 1975, the FCC established a registration program for data and ancillary devices which met the technical standards set forth in the FCC rules. The PCA requirement was continued as to such of those devices which did not meet those technical standards. In 1976, the registration program was extended to traditional tcrminal

terminal equipment, such as PBXs, Key Systems, and "Main Station" telephones. The registration program for ancillary and data equipment went into effect in June, 1976. The Phonemaster was registered under that program and from that time on a PCA was no longer required to attach the Phonemaster to the telephone system.

These decisions ended the "PCA era." These developments toward a competitive business, together with other factors in the industry (i.e., long distance competition, etc.) eventually culminated in the splitting apart of the Bell System, effective in January, 1984. The developments related above, and others, were a part of massive change in government policy toward the regulated telephone business. Until the late 1960's, it was widely accepted that a utility with a "natural monopoly" would have the abuses which can arise from monopoly

handled by government regulation. A change in policy took place between the late 1960's and the mid-1970's in this respect. Competition as the regulator of price and service came to be utilized as an important element, along with regulation, in the telephone field. The basic impetus of the change in policy was the theory that improvements in technology in the electronics field should not be entrusted only to a regulated monopoly, but, instead, the public interest in having a variety of devices and facilities available could only be served by allowing the entrance from the outside of such devices into the telephone system. The "Phonetele story" is but one small chapter in the revolutionary change which accompanied the change in government policy. AT&T, peopled as it was with employees who had spent their careers in making quality telephone service available to all on an

affordable basis, did not fully accept the premise that competition could improve rather than degrade the quality and cost of its service to the public. Whether they are and were right or wrong still will have to be played out on the pages of history. It is, however, the Court's finding that the AT&T resistence to the registration-certification part of the change was not based upon anti-competitive motivations, but rather on its belief as to how best to provide effective and economical telephone service to the public. Its technical concerns were based upon factual and engineering imperatives known to it and recognized as legitimate by the regulators. It is, therefore, not subject to damages by insisting that the Phonemaster between 1970 and 1976 be attached to the system through a protective connecting arrangement.

The Court recognizes that the conclusions it has reached were different than the conclusions reached by the jury in the Litton case.[21] The jury in Litton found that the PCA requirement was anti-competitive in intent. The Litton case involved a PBX product which directly competed with the PBXs of the Bell System. In the sense that terminal equipment competing with the Bell System's product was involved in the Litton case, it is different than this case, involving as it does ancillary equipment without, for the most part, competing Bell System equipment. However, it must be recognized that the jury decision in the Litton case is not consistent with this Court's decision in this case. The Second Circuit Court of Appeals upheld the jury's verdict in the Litton case as being supported by substantial evidence. To the extent that the Noerr-Pennington doctrine

was involved, the Second Circuit Court of Appeals affirmed the finding that the opposition to registration-certification before the FCC was "a sham" and therefore not protected by the First Amendment. This Court's different conclusion is based upon its application of the Ninth Circuit Court of Appeals test to the factual situation found here. Believing that the preponderance of the evidence is different than that found in the Litton case, the Court has come to a different conclusion.

9. Phonetele during the PCA era: As set forth above, the Court has determined that the post-Carterfone tariffs did not violate Section 2 of the Sherman Act. Simultaneously with the filing of the post-Carterfone tariffs, BOCs filed complementary tariffs with the various state regulatory bodies. Thus the PCA requirement for the attachment of ancillary equipment was made

mandatory through tariff in each local jurisdiction.

Plaintiff contends that the implementation of the PCA requirement as to it was invalid under Section 2 for a group of other reasons pertaining to the relationship between Phonetele and Bell System. It is thus necessary to turn from the macro-regulatory scene to the micro-regulatory scene to examine the particular contentions of Phonetele in this respect.

Phonetele makes a number of contentions, the most important of which is that at various times and places, PT&T and AT&T did not make available to it suitable PCAs. It is contended that this alleged failure was done to prevent or hinder access of Phonetele to the market, and was done despite knowledge that the Phonemaster created none of the four harms and that s special registration program for it should

have been developed.

It is further argued that a delay or failure to provide an appropriate PCA at nominal or minimal charge, even without anti-competitive intent, is a Section 2 violation because it involves a use of monopoly power to exclude a product from the market.

Phonetele entered the call restrictor market in early 1971. Phonetele had taken preparatory steps in late 1970 to enter this market, and in November, 1970, had inquired of PT&T, and later AT&T, about the availability of a PCA. At this time, the PCA requirement had been in national and local tariffs for about a year and a half.

When Phonetele notified AT&T of the need for a PCA, an AT&T engineer came to California in December, 1970, and consulted with Phonetele's and PT&T's engineers. The AT&T engineer estimated that the design

work would take approximately one month (i.e., to sometime in January, 1971). The design of a PCA for Phonetele was assigned to a Bell Labs engineer who produced a schematic drawing of the design of a PCA. The Bell Labs engineer designed the PCA (then denominated the CTD) in a rush to attempt to meet the asserted time necessities of Phonetele. He designed the PCA so that it used "off the shelf" electronic components and could thus be assembled and tariffed quickly and cheaply. The design was forwarded to PT&T's engineer in charge and the schematic drawing was delivered to Phonetele for its comments on March 3, 1971. Phonetele responded about a month later, indicating that the schematic drawing looked usable to Phonetele. This schematic drawing was later used by PT&T to produce the PCA used behind the Phonemaster in California for the next five years,

denominated the "ZZAGM."

The management at Phonetele disputed then, as it continues to do to this date, the need for a PCA in connection with Phonemaster. The first installation of the Phonemaster did not bring it into conflict with PT&T, however. The first installation was in the territory of General Telephone. General Telephone did not then have a PCA available (it subsequently adopted what was essentially the ZZAGM), and so Phonetele "hardwired" its then version of the Phonemaster directly to the telephone circuits. General sought to disconnect, and this led to the earliest clash between Phonetele and the telephone industry, with the forum being the California Public Utilities Commission (CPUC). Phonetele took the position that no PCA was necessary, and in any event it certainly was not necessary if General Telephone could not come up with a PCA. In April, 1971,

the CPUC agreed, ordering General not to insist on a PCA in what was the regulatory equivalent of a preliminary injunction.

Thus, when it came time in March or April, 1971, to tell PT&T that the ZZAGM was satisfactory to Phonetele, Phonetele announced that it had take a "fundamental change of position" and would insist that no PCA need be attached behind the Phonetele. Thus started a prolonged period of litigation between Phonetele and PT&T in the CPUC. Phonetele precipitated the action in mid-1971 by hardwiring Phonemasters to PT&T lines and moved to join PT&T in the litigation with General Telephone. The subject of the litigation was the validity of the General and PT&T tariff requirements that ancillary equipment electrically connected must be connected through a PCA. During the course of the CPUC litigation, Phonetele maintained its posture that it need not

connect through a PCA, and turned down for this reason PT&T's offer in May 1971 to test the ZZAGM with the Phonetele equipment. Management of Phonetele took the position that it would do nothing which might prejudice its position that no PCA was required. While the CPUC decision was pending, Phonetele desired to display the Phonemaster at a trade show in October, 1971. At this point the irresistable force (Phonetele) came into direct collision with the immovable object (PT&T). Phonetele moved its equipment into the trade show and "hardwired" it to PT&T telephone lines. PT&T appeared with the ZZAGM prepared to install it and test it on the spot at the trade show. Phonetele declined to have it so installed and tested. PT&T declined to continue phone service without the installation of a PCA, in accordance with its tariff. Impasse resulted. PT&T disconnected telephone service at the

trade show. PT&T's disconnection was proper if its tariff was valid, the subject of the then litigation between Phonetele and PT&T.

The next month, in November, 1971, the CPUC ruled that the PCA requirement was valid, that PT&T could insist upon it, and reversed its prior order to General to connect without a PCA.

Phonetele complains about the way the PUC litigation was managed from the PT&T end. It alleges that incomplete information was submitted, that falsehoods were knowingly made, and that in other ways the telephone company position was unfairly presented. The Court finds to the contrary. The PUC litigation was, in microcosm, a replay of the arguments before the FCC, except as it applied to the Phonemaster. The litigation emphasized a subject which has been present throughout this controversy: i.e., whether the focus is on the

Phonemaster as a particular ancillary device, or, on the other hand, is on the generalized need to require PCAs whenever non-Bell System ancillary or terminal equipment is electrically attached. It is apparent that at that time the CPUC accepted PT&T's position. (At a later time, starting in 1973, it started its own study on certification-registration, which paralleled the FCC studies.)

In the course of the CPUC litigation, the CPUC made an order, apparently to be temporary pending its final decision, that no charges could be made by PT&T for the use of the ZZAGM. For reasons obscure to the Court, this order was never terminated. Thus, until the demise of the PCA with the advent of registration, Phonetele's customers were not required to pay for the use of the ZZAGM, which, therefore, was provided free of charge by PT&T. (This circumstance was a

financial windfall for Phonetele, since it did not need to and did not include in its circuitry the protective electronics which were also provided by the PCA. Ironically, this means that had Phonetele's basic position regarding registration been accepted, the cost of its equipment would have been increased by the cost of the protective devices otherwise provided by the ZZAGM. This is not the only irony in the case.)

It will be noted that the designation for the original paper version of the PCA designed for use with Phonetele equipment was the "CTD." During the tariffing procedures with the CPUC, the designation was changed to "ZZAGM." The reason was as follows: At the time Phonetele was taking the position that no PCA was required, the designed PCA was being reviewed by the so-called "Erickson Group," a multipurpose intra-AT&T task force group established to

review both the engineering and the tariffing and regulatory problems of PCAs. This group was established in the AT&T Headquarters in New York and was given overall corporate responsibility to supervise the technical and financial aspects of the PCA requirements under the AT&T and BOC tariffs. The group was named after its supervising executive, Mr. Donald H. Erickson. In its review of the Bell Labs design for the CTD, in comparing it with the principal use envisioned for it (Phonemaster), the Erickson Group noted two things. First, the Phonemaster was an "interpositioned" piece of equipment, meaning that it was to be inserted in the telephone network between Bell System provided terminal equipment and the remainder of the Bell System network. This came about because the primary use envisioned for the Phonemaster was to be inserted in the telephone lines behind the PBX. Secondly, from

an engineering standpoint it was determined that the originally designed CTD did not provide sufficient protection against two types of degregation to telephone service, known as "blockage" and "glare." The interpositioning, blockage, and glare problems will be discussed below. The result was that the Erickson Group disapproved the original design of the CTD as a national standard for PCAs in connection with call restriction equipment. In effect, the design was sent back to the drawing boards for further work by Bell Labs (in connection with the technical faults) and, in any event, interpositioning was at that time disapproved by AT&T.

The interpositioning issue apparently was not involved in litigation during this period. However, there was a substantial debate within AT&T itself as to what their position should be on interpositioning. The problem of interpositioning had not been

in Carterfone and it appears not to have been addressed by the post-Carterfone tariffs. At that time, AT&T assumed that ancillary equipment would be attached in front of any AT&T equipment, rather than in the middle of the line between pieces of Bell System equipment. The Phonemaster and other call restriction equipment was a rare exception. The Erickson Group saw inter-positioning as a doctrinal problem to be resisted. The reasoning was that, traditionally, the telephone company had end to end responsibility for operation of the telephone network. While accepting the new concept that telephone service started with a PCA when non-Bell System terminal equipment was attached, the doctrinal position was that this responsibility could not be maintained where Bell System equipment was electrically placed on either side of a non-Bell piece of equipment which was

"interposed." With the responsibility for operation of the network, and the imposition of full responsibility for maintenance and financial responsibility on the network as a whole, the Erickson Group's position was that such could not be maintained if responsibility was shared by a piece of interpositioned equipment. Neither AT&T nor the BOCs attempted to implement this doctrinal position by tariffs which explicitly prohibited interpositioned equipment. However, the position was taken at AT&T (but not PT&T) that such should be resisted. This position was maintained by AT&T until 1972, when the policy was reversed and interpositioned equipment was allowed. The internal debate within AT&T never became public or known to plaintiff so far as the record reveals.

In California, PT&T faced an immediate regulatory problem with respect to

Phonetele's challenge to the PCA rules. PT&T determined not to attempt to establish AT&T's anti-interposition policy with the CPUC. Instead, it developed, manufactured, tariffed, and installed the ZZAGM, which was PT&T's version of the original CTD schematic drawing. In doing so, it used off-the-shelf Western Electric parts and assembled them in PT&T workshops. When the California tariff was filed, the PCA was redesignated as the ZZAGM. In Bell System terminology, the "ZZ" means a device tariffed by local BOC, and not tariffed nationally. "AGM" was the PT&T designation for the PCA. Phonetele claims that the reason for the change in designation to "ZZAGM" was never explained to it and that PT&T was guilty of fraud and deception before the CPUC in not explaining that the ZZAGM was not a nationally standardized device. It is true that the interpositioning problem being debated within AT&T was not explained to the management of Phonetele or

to the CPUC. However, there is nothing false about the explanation given for the change of designation. The ZZAGM was essentially the same as the CTD; thus, the explanation that the device was the same as originally designed but with a different designation is true. Management of Phonetele also contended that AT&T and PT&T "concealed" from Phonetele that the ZZAGM was not a nationally accepted PCA. The Court finds to the contrary. The question did not come up until Phonetele desired to expand its sales to a national level in 1973. At said time, it was explained that the ZZAGM was not a nationally accepted PCA, but the revised CTD was then available.

Blockage and glare are two technical problems with the use of phone restriction equipment. While the technical description of the problem will not be set forth here, in general the two problems occur with the opening and closing of the telephone line

in the Phonemaster when it is called upon to reject an outgoing call. Depending on the timing of the switching on and off of the telephone circuit in the Phonemaster, an incoming call (on a two-way circuit--the problem does not exist on a line dedicated to outgoing calls only) can be blocked even though the circuit should be open to receive incoming calls. This problem is called blockage or "ringing into an open circuit." In addition, if the line is closed before the user hangs up, the incoming call can push right through the PBX to the wrong extension, thus causing misconnections, called "glare." Blockage and glare cannot be eliminated altogether, but careful timing on the disconnect sequence can greatly minimize the occurrence of blockage and glare. The natural design of the Phonemaster made it subject to these two phenomena. It is unclear to the Court

whether the two phenomena should be rated as subdivisions of "improper network signaling" or be considered as additional harms which degrade telephone service. The two phenomena do not cause any particular physical harm to the telephone network. However, if present in significant numbers, they would degrade the quality of service provided by the telephone system by causing inability to complete calls which should be able to be completed, or by misdirecting calls to unintended destinations, both of which may result in frustration and charges to a customer who must replace the call. The original CTD (subsequently manufactured as the ZZAGM) had no protection against blockage or glare. The designer at Bell Labs contemplated that the manufacturer (Phonetele) would put in a necessary delay to eliminate glare and did not originally recognize the blockage problem. Thus, for

the two reasons, one doctrinal and one engineering, the original CTD was not standardized as a network approved product.

PT&T, however, was under the litigation gun. It felt that the litigation pressure applied by Phonetele required it to come up immediately with a PCA, or run the risk of having the PCA requirement disallowed entirely by the CPUC. PT&T therefore approved ZZAGM despite its deficiencies and tariffed it for use behind the Phonetele and other similar devices. Plaintiff contends that PT&T thereby required it to use a "defective" PCA, and that the only reason it did so was to inhibit the use of the Phonemaster. The Court does not accept this argument. First, Phonetele's customers never had to pay for the PCA; such was entirely on PT&T's head. Secondly, the ZZAGM did protect against most of the major harms it was designed to protect against. It prevented

the entry of high voltage into the telephone lines, regulated the amplitude of the telephone signals and was designed to prevent "longitudinal imbalance." (That for some years it did not correct the latter in fact was another irony in the case.) It did not correct blockage and glare.

The principal basis of Phonetele's charge that the ZZAGM was "defective" and "worthless" came from its failure from 1971 to 1974 to correct longitudinal imbalance, and in fact, itself added to the longitudinal imbalance created by the Phonemaster. The additional longitudinal imbalance added by the ZZAGM came about as follows: The original design of the CTD (hereinafter ZZAGM) contemplated that the Phonemaster would be attached by a six-prong plug. Management of Phonetele vigorously resisted this design and insisted upon a four-prong plug. Phonetele apparently insisted on the

four-prong plug because it foresaw the elimination of the PCA as a requirement and wanted to be able to connect through a standard four-prong plug to a simple terminal block. Assuming the Phonemaster is to be used with a PCA, a four- or six-prong plug is equally acceptable from an engineering standpoint. PT&T reluctantly acceded to Phonetele's demand and converted the ZZAGM to four-prong use. In doing so, however, an engineering error crept into the design, uncaught by PT&T until 1974. The engineering error caused longitudinal imbalance in excess of that already present in the Phonemaster. The effect of longitudinal imbalance was the potential for noise on the telephone lines of others. It is a transistory harm occurring from time to time in different situations. It is of relatively minor significance when not occurring in a mass of telephone devices; nevertheless,

the phone company has expended substantial time and resources to prevent the creeping infiltration of longitudinal imbalance into its lines in the interests of quality service. One of the ironies of this case is that the ZZAGM worsened rather than corrected that situation prior to correction of the ZZAGM. A PT&T engineer, on a routine check for other problems, discovered the longitudinal imbalance, reported it to PT&T management, and it was corrected.

Phonetele heaps scorn upon the ZZAGM as a worthless device. The Court finds that it was not worthless, despite its faults. It provided protection against several of the harms. To the extent that it did not provide full protection, the ZZAGM was not willfully designed to injure the Phonetele competitive position. In fact, if anything, it benefitted Phonetele's competitive position for the reasons stated above. The Court

declines to find any antitrust significance in the asserted deficiencies of the ZZAGM.

As the ZZAGM was used with successive generations of Phonemaster models, it needed adjustment from time to time. PT&T redesigned it to meet the new requirements. Thus, the ZZAGM went through several model changes. It continued, however, to be used without charge to the customer until the PCA requirement was dropped. Most of the Phonetele sales of Phonemasters were made with ZZAGMs attached. The PCA requirement for sales of the Phonemaster in California never adversely affected Phonetele's sales.

It is now necessary to turn to the national scene. AT&T continued the development of the CTD. It was modified to take care of the technical problems found in the original version of the CTD. The final version developed in 1972 will be called the "final" CTD to distinguish it from the

original circuit design drawn by Bell Labs in 1971. The final CTD was designed to solve the problems of blockage and glare, with the use of an electronic technique called "battery reversal." The final CTD was designed to be used in connection with a whole family of call-restricting equipment, of which the Phonemaster was a prominent but not exclusive representative. The final CTD was ready in 1972, long before Phonetele was ready to attempt to expand its sales nationwide. Phonetele makes a claim that it was ready to "go national" as early as 1973, but could not because of the absence of a suitable PCA. The Court finds to the contrary. Phonetele, up to a point, assumed that it could use the ZZAGM nationally and was informed sometime in 1972 or 1973 that this was not the case. (There is a dispute in the testimony about this, which is not resolved because no reason to

resolve it exists. Mr. Feiner, President of Phonetele, states that he was not told that ZZAGM was not a national standard until he requested national hookup of it. Mr. Black, PT&T's engineer in charge of the Phonetele account, states that he told Mr. Feiner as early as 1971 that the ZZAGM was only a California product.)

The dispute is not resolved because it is not necessary to resolve it. AT&T had developed the final CTD and it was ready in 1972. Phonetele's first customer for the Phonemaster outside California was obtained in 1974. That customer could have been "hooked up" through the CTD at that time or at any time earlier when Phonetele was ready to make a sale outside of California.

However, doctrinal problems intervened. Phonetele, aside from taking the legal position in CPUC litigation with PT&T, that no PCA was required at all, also

took the backup position that if a PCA was to be required, no changes would be made in the Phonemaster to accommodate it to a general purpose PCA. In other words, Phonetele's position, from which it never receded, was that it was the obligation of the Bell System to provide a PCA which worked with its product without any accommodations by Phonetele to the problems of AT&T. Phonetele's position, then and since, was that with AT&T's monopoly power over the phone network, and with its insistence on a PCA, it, not the manufacturer of the ancillary device, had to conform the PCA to the product. It further took the position that AT&T had to be ready with the PCA whenever and wherever Phonetele was ready to sell, with or without notice. Thus arose the dispute about the final CTD. The final CTD was workable with the Phonemaster. However, because of the technical basis on which it

worked, a dial tone or busy signal needed to be substituted for the da-da-da-daaah sound produced by Phonemaster to inform the telephone user that his call had been restricted. This change required minimal changes in the Phonemaster, but Phonetele refused to cooperate, citing its doctrinal position that AT&T had the obligation to provide a PCA to fit its designed equipment without change. In addition, Phonetele complained that the CTD was not usable behind key sustems, which it was not. It demanded that a PCA be produced to work behind key systems. In addition, the 4 wire, 6 wire dispute was renewed. AT&T also repeated its request that Phonetele build into the Phonemaster a 1.5 second delay following restriction to eliminate the glare problem. This suggestion had been in the Bell Labs design since the beginning, and was consistently refused by Phonetele. These

differences were discussed in a series of meetings between Phonetele personnel and AT&T personnel in mid-1973. AT&T, despite its strongly felt position (to this day) that Phonetele's demands were unreasonable, designed two new PCAs on a crash basis. The CTH was designed to accommodate the use of the Phonemaster behind a PBX. The KTX was designed to accommodate a Phonemaster behind a key system. Phonetele attained its first non-California customer (the New York Times) in 1974. A PCA was provided on a "special assembly basis" (meaning that it had not been finally approved) behind the New York Times installation. Phonetele, however, did not have other non-California sales until 1976. Of course, from the above history, it is noted that the registration rules came into effect in 1976 and the PCAs were therefore obsolete therafter. No KTX PCA was ever used. The only CTH used was

the one constructed on a special assembly basis for the New York Times.

Phonetele claims that it was delayed in entry into the national market by the failure to have a PCA ready. The Court rejects this contention. The Court finds that the CTD was a properly designed PCA for universal use behind toll restriction equipment. The minor modifications required of the Phonemaster did not prevent its national use with the CTD if there were sales nationally to be made. Applying the rule of reasonableness, Phonetele's insistence on the use of the first four notes of Beethoven instead of a busy signal is not sufficient reason to keep it out of the national marketplace. Neither was the ideologically based refusal to make other minor modifications. AT&T met the rule of reason in having the CTD available when Phonetele needed it. The Court further finds that Phonetele was

not ready for national sales in 1973 or 1974. At that time, Touch-Tone telephones were starting to come into prominent use, and Phonetele did not have equipment suitable for use with Touch-Tone telephones until 1976. It is true that AT&T did not have available a PCA usable with a key system telephone service until the KTX was developed. However, Phonetele did not have any key system customers at that time. As pointed out before, only rare customers would use a Phonetele behind a key system telephone service because of the uneconomic application. Because no such sales were available prior to the availability of the KTX, no liability can be predicated thereon, even if AT&T had a theoretical obligation to have such a PCA available.

Phonetele also complains about the cost of the CTD and CTH. The cost was approximately $4.00 a line per month, which

was significant. The net cost to Phonetele's customers, however, was far less since the protective circuitry in the PCA need not be repeated in the Phonemaster itself, and was not. The additional costs, therefore, for the PCA over and above a Phonemaster with protective circuitry designed into it, is minimal though not quantifiable on this record. Such extra cost is justified by the necessity for physical protection of the phone network.

The Court concludes that the PCA requirement, national and local, was not a Section 2 antitrust violation, either from a macro-regulatory or micro-regulatory viewpoint. In general, and as implemented with Phonetele, the PCA requirement met the standards posited above in the Court of Appeals opinion. Judgment will, therefore, be entered for the defendants on all contentions having their basis in the

requirement that a protective connecting arrangement be used in connection with the Phonemaster between 1970 and 1976, when the requirement was dropped.

10. Noerr-Pennington doctrine: AT&T has made a major point out of arguing the Noerr-Pennington[22][23] doctrine. The Noerr and Pennington cases provide protection to a person or business advocating certain steps to be taken by regulatory agencies. The protection is based on First Amendment principles. Under the Noerr-Pennington doctrine, a business cannot have antitrust liability for what it asks a regulatory agency to order, or for other positions taken before a regulatory body. There is an exception to the doctrine; if the positions taken before a regulatory body were a "sham," without any expectation of success and with an intent to use the regulatory body as an anti-competitive tool, then the

immunity does not apply. The Bell System took no sham positions before the regulatory bodies (FCC or CPUC) here. The Bell System believed what it was urging, had a basis (though ultimately rejected in the case of registration) for what it was urging, and sincerely attempted to convince the regulatory bodies as to what was in the best interests of the nation and the Bell System (the latter thought the two were concurrent). Having said that, the impact of the Noerr-Pennington doctrine in this case is minimal. The position taken in the FCC from 1973 to 1976 in opposition to a registration program is protected by the Noerr-Pennington doctrine. However, the other side of the coin, the keeping in effect of a PCA requirement in a tariff, is not protected by Noerr-Pennington. Insofar as plaintiff urges that AT&T should have adopted a registration program on its

own, the refusal to do so would not be protected by Noerr-Pennington. Insofar as the plaintiff urges that registration was a better alternative than the PCA, a telephone company's disbelief is not protected by Noerr-Pennington. It appears, therefore, that Noerr and Pennington play a very small role in the case. The Court finds the doctrine applicable, and thus no antitrust liability could be hinged upon the opposition in the regulatory bodies to a registration program. The large picture, however, remains open to examination under the tests prescribed by the Court of Appeals.

11. The Call Controller as a "fighting ship": Aside from its principal arguments based upon the PCA requirement, Phonetele asserts a separate violation of the Sherman Act in the PT&T development of a toll restrictor called the "Call Controller." It is the Phonetele contention that

the Call Controller was developed for the purpose and effect of providing competition to the Phonemaster in the relevant market. The Court finds these contentions are not borne out by the facts.

As Phonetele was preparing to enter the call restriction market in 1970 and 1971, there were already competing devices on the market. Various BOCs had tariffed call restrictors manufactured by Stomberg-Carlson, North Electric, and Mitel. Each of the call restrictor devices had been tariffed by various BOCs, but were not a universal offering through the Bell System. The competing devices were, by and large, electromechanical restriction devices designed to operate behind PBXs then common in the market. They had more limited capabilities than the ultimate Phonetele product. They were initially successful, but as telephone equipment increased in complexity,

the costs and limitations of most of those devices presented market barriers to their use. These devices, by and large, had only three-digit programmable capacity and were therefore not usable in all of the more complicated configurations addressed by Phonemaster. In addition, most BOCs, by the time Phonetele entered the market offered simplified restriction capacity on a "0 and 1" basis. Such simplified toll restriction had the effect of restricting the use of the telephones it served to local zone calls, preventing the user from dialing long distance numbers or the operator to complete long distance calls.

In the late 1960's, PT&T's marketing staff detected a need for a low-cost toll restrictor. The contemplated devices were for three-digit restriction and primarily for use in hotels and motels to prevent the customer from making other than local zone

(non-message unit--non-long distance) calls. In 1969, a PT&T engineer recommended the development of such a three-digit call restrictor designed on the same principles that the Bell 761-PBX system used. At that time, some PBXs had, more fully developed later, certain call restriction capability. The recommendation was for the development of a system similar to the then 761-PBX to be used behind PBXs which did not have that system. The recommendation was approved in the middle of 1971, at the very beginning of the Phonetele controversy with PT&T. The Court finds that the suggestion and approval of the PT&T telephone restrictor, denominated the "Call Controller," was not prompted by the entry of Phonetele in the market. Indeed, the recommended Call Controller envisioned a less sophisticated market, and was designed to be a low cost and low capacity toll restrictor, which would place it

in the market below the aim of Phonetele, which had far more complex capabilities and thus higher cost. The personnel at AT&T behind the development of the Call Controller were not involved in the Phonetele controversy. PT&T ultimately licensed its design to Leh-Mah Corporation for manufacture. In 1973 or early 1974, PT&T attempted to tariff the Call Controller. Phonetele opposed the tariffing. Ultimately, an agreement was reached between PT&T and Phonetele that both the Phonemaster and the Call Controller would be tariffed by PT&T.

The Call Controller as finally tariffed had one level, three-digit programmability behind a PBX system utilizing four to twenty trunks. The Phonemaster had seven digit programmability, with four levels of restriction and could accommodate up to thirty-two trunks. Because of the increased complexity of the Phonemaster, it was

designed to be used behind larger PBXs than the Call Controller was designed to be used with. Later, Phonetele designed a new model of the Phonemaster, which was Touch-Tone compatible (the Call Controller was Touch-Tone compatible from the beginning) and which provided some overlap in competition with the Call Controller. However, for all practical purposes, the Call Controller was designed for a smaller, less complex PBX system and thus was only marginally competitive with the Phonemaster. In 1977, PT&T withdrew the tariffing of the Call Controller. At this time, PT&T had experienced quality control problems in the Call Controller as manufactured under license by Leh-Mah. In addition, a new Phonemaster product (Model 2010) provided a Touch-Tone service with low trunk capacity for the small PBX market.

Leh-Mah applied for BSPPD approval of the Call Controller, with the intent it be distributed by other BOCs. However, this approval of the Call Controller was never granted. The Call Controller thus never entered the national market. The Court find finds that the Call Controller was never a "fighting ship" intended to hurt Phonetele's ability to compete in the market. Aside from marginal overlap, the two devices--the Phonemaster and the Call Controller--were designed for different segments of the call restriction market. The Call Controller was developed to meet a limited area of the toll restriction market. It had limited use, and that use was not the principal use contemplated by the Phonemaster. The Call Controller was used in California only and was not tariffed until the Phonemaster itself was tariffed. When Phonetele provided a product in fact competitive with the Call

Controller (i.e., a Touch-Tone device with low trunk capacity), PT&T, presumably for competitive reasons, withdrew its tariff on the Call Controller. The Court concludes that the Call Controller was not an anti-competitive "fighting ship" impermissibly used by a monopoly for anti-competitive purposes.

It should be noted parenthetically that as a condition of tariffing of the Phonemaster in 1974, PT&T required that certain deficiencies (as perceived by PT&T) be corrected. The Phonemaster's power supply was required to be UL listed. The problem of longitudinal balance was corrected. The time delay requested by Bell Labs in its original schematic was incorporated to reduce the glare problem. And a "forced disconnect" was added to protect against or minimize the blockage problem. Phonetele, to obtain PT&T tariffing, made these long

requested corrections in the Phonemaster and it was thereafter tariffed and sold by PT&T.

12. National marketing problems in BOC sales of the Phonemaster. When Phonetele started selling its product in 1971, it did not contemplate selling it through the Bell System. Up to 1974, Phonetele concentrated on selling the Phonemaster independently of the Bell System. In 1974, about the time this lawsuit was commenced, Phonetele had a basic change in its marketing policy. It applied for and received (as stated above) PT&T tariffing of the Phonemaster. Thereafter, the great majority of Phonetele sales were made by PT&T. In 1975, Phonetele attempted to expand its sales by utilizing the other BOC sales facilities. In the meantime, in 1974, AT&T established its "Bell System Purchased Productions Division" (hereinafter BSPPD). The

stated purpose of the BSPPD was to investigate non-Bell System products and evaluate them for the BOCs. If the product was approved, a national marketing contract was offered setting forth the terms on which the BOCs would, if they desired, purchase the independently manufactured products for tariffing and leasing by the BOCs to ultimate customers. The stated purpose of the BSPPD was to open up the Bell System to products of independent manufacturers and provide the BOCs a centralized evaluation which would not have to be repeated in each BOC.

Plaintiff contends that the creation and operation of BSPPD was an anti-competitive elaborate trap designed to exclude from rather than include competitive products in the market. No evidence supports this contention and the Court rejects it as merely pejorative. In 1975, Phonetele

sought BSPPD's evaluation and approval of its product. BSPPD at first rated the Phonemaster as "not suitable." On Phonetele's protest, this rating was upgraded to "conditionally suitable." In April, 1976, Phonetele placed on the market its new 2020 and 2040 models, which had newly acquired Touch-Tone capability. BSPPD rated the new models as "suitable" for BOC tariffing and a national purchasing contract was entered into.

The national purchase agreement did not obligate any BOC to buy and tariff a product; it merely indicated suitability for telephone company use and set forth the terms on which the item would be sold to the BOCs.

Phonetele made a major effort to induce the BOCs to buy and tariff the Phonemaster. This effort had only limited success. Only PT&T, New York Telephone, and

New Jersey Bell, among the BOCs, tariffed the Phonemaster. All three had net losses in their marketing of the Phonemaster.

Phonetele makes apparently contradictory arguments:

a. Phonetele argues that the failure of the bulk of the BOCs to tariff the Phonemaster was a "group boycott."

b. It argues that the willingness of PT&T, New York Telephone, and New Jersey Bell to tariff the product was a plan to prevent or limit sales of Phonemaster within the territory of those companies. Both contentions are rejected.

With regard to the declination of most of the BOCs to tariff and market the Phonemaster, the limitations of the Phonemaster market, as set forth at the beginning of these Findings, must be recognized. The Phonemaster has it primary economic utility in zone or message unit areas where

additional charges are imposed upon the customer for comparatively short distance calls. These are basically the large urban areas of the country in which zones and area codes are highly compacted. In such areas, the phone companies provided so-called "foreign exchange" service, wherein a customer could purchase at local call rates lines to areas in another zone, thus keeping the customer's message units to a minimum. In other areas, and for long distance calls, direct line service was provided to other area codes by co-called WATS lines provided at fixed prices by the BOCs, which prices were advantageous if certain numbers of calls were made. The Phonemaster had its greatest utility in requiring that foreign exchange and WATS lines be used where available. It had the additional advantage of preventing or restricting the calls to expensive areas where

the customer's policy was that employees should not call. In addition, the Phonemaster's economic use was limited to use behind electromechanical PBXs which had been the staple private phone exchange device into the middle 1970's. In the 1970's, however, more sophisticated PBXs were coming on the market, sold not only by the Bell system, but by manufacturers independent of the Bell System. These newer PBXs were solid-state and incorporated within their workings sophisticated programmable toll restriction capabilities among other features, much as provided by the Phonemaster. Thus, as customers gradually switched over to the more modern PBXs, the Phonemaster became more and more obsolescent. The Phonemaster therefore became a device primarily to be used by customers keeping the older equipment. In addition, in the early 1970's, the newer telephones

(provided both by the Bell System and by independent manufacturers) were turning to Touch-Tone service which was more convenient for the customer than the older rotary dial telephones. Until 1976, the Phonemaster was not compatible with Touch-Tone use. It follows that while the Phonemaster was a useful device in the circumstances for which it was most economically used, as telephone equipment advanced, it became more and more obsolete. As Phonetele attempted to enter the national market these trends were more and more operating against it. Phonetele believed (and believes to this day) that there is a "vast market" in the country for its product. It does not accept that its failure in the national market was caused by natural limitations of the market rather than the predatory activities of AT&T.

Most of the larger BOCs investigated the Phonemaster following its listing by BSPPD and at Phonetele's urgent request. The majority of the BOCs received marketing advice that there was an insufficient market to justify tariffing the Phonemaster. Tariffing a device requires a significant investment by a BOC. Its sales and engineering personnel must be trained in the installation, operation, use, and maintenance of the device. A significant inventory must be acquired and maintained. Legal costs in justifications to local regulatory bodies must be invested. These costs require a certain substantial capital investment when a new product is to be tariffed. The bulk of the BOCs determined that in their territory there was an insufficient market for the Phonemaster to justify tariffing it. The Court rejects Phonetele's contention that an anti-competitive

conspiracy among the BOCs caused the majority of the BOCs not to tariff the Phonemaster. The Court concludes that the preponderance of the evidence is that the majority of the BOCs which did not tariff the Phonemaster did so because of their acceptance of their marketing department's recommendation that there was an insufficient market to justify the tariffing.

Phonetele also complains of what it contends is non-support by New York Telephone and New Jersey Bell after the Phonemaster was tariffed by those BPCs. Each tariffed the Phonemaster over the projections of their marketing departments that an insufficient market appeared. In New York Telephone, upper management overruled the marketing department and determined to tariff the Phonemaster. It may be that the aggressive litigation being pursued by Phonetele at several levels was

an intimidating factor to the agreement of New York Telephone to tariff the Phonemaster. Plaintiff contends that New York Telephone had as its primary objective the tariffing of the Phonemaster in order to inhibit its sales in New York Telephone's territory. No evidence supports this contention and the Court rejects it. New Jersey Bell also tariffed the Phonemaster when it discontinued the Stromberg-Carlson tariffing in approximately 1978. However, New Jersey Bell only actually sold a limited number of Phonemasters in its territory.

Phonetele claims that sales policies of the BOCs inhibited the sale of the Phonemaster. This contention founders on several grounds. First, the BOCs had no obligation enforceable on antitrust grounds to attempt to sell the Phonemaster at all.[24] Second, if the BOCs did tariff the Phonemaster, they had no obligation to provide

it with sales support which they, in their best business judgment, did not believe was justified.

Here, Phonetele complains of several sales practices of the BOCs. First, it claims that the BOCs sold the Phonemaster on "demand only." It appears true that, at least before Phonetele's national sales effort, BOCs did not affirmatively push the sales of toll restriction equipment. The basic reason is probably that the Bell System was not in the business of preventing phone calls from being made. However, the preponderance of the evidence is that phone company salesmen responded to requests for toll restriction equipment when requested by the customer, and that this included the Phonemaster when it was suitable for the customer's needs. Next, plaintiff contends that starting in the mid- or late 1970's, the Bell System began rating its salespersons'

efficiency (and thus apparently affecting salary levels) by comparing the salesperson's ability to improve sales over former levels in that salesperson's area. Phonetele's suggests that this led to discouraging salesmen from selling equipment, such as the Phonemaster, which would have the effect of lessening toll charges. There is no convincing evidence that a sale of a Phonemaster (which would increase sales to the extent of the tariffed costs of the Phonemaster) would necessarily decrease a salesperson's overall income. In any event, the salesperson would be motivated by the necessity to meet the customers' needs so as to prevent the loss of the customer to the sales efforts of non-Bell suppliers, which would produce a decrease in revenues far exceeding those caused by a toll restriction device. In addition, the Bell System was giving priority to the sales of new equipment,

such as solid-state PBXs which, among their many advanced features, had toll restriction capability which made Phonemaster (usable only with an older style PBX) obsolete. The Court rejects the contention that BOC sales techniques had any part in the failure of the Phonetele national sales efforts. Lastly, Phonetele complains of the "migration" sales policy of Bell System marketing. The idea behind the "migration" policy was to attempt to induce customers to buy new and upgraded equipment in place of older equipment, including PBxs behind which the Phonemaster could operate. Plaintiff contends that this strategy is counter-productive to the sale of the Phonemaster. So it is. However, there is no antitrust violation in this. The revolution, of which Phonetele is a part, forced the Bell System to become aggressive in its sales policies and to compete with outsiders. Like GM, Ford, and Chrysler, it must aggressively market its most profitable

products in direct competition with outsiders. The Carterfone revolution forced AT&T out of the nest, and this revolution, which created Phonetele, also sounded its death knell when the product became obsolescent.

The New York and New Jersey Bell Companies had no obligation to market the Phonemaster in the first place, and, having done so, had no obligation to provide it the so-called "type 1" support given to the premier Bell System products. Phonetele was perfectly free to compete in the market with its own sales force, its own leasing companies, and its own personnel, as they did with relative success in California between 1971 and 1976.

Phonetele contends that the whole BSPPD and local tariffing concept is a sham. It contends that AT&T had no intention to allow foreign attachments into its network,

and that, using a spider and web technique, the whole purpose of BSPPD was to lure unsuspecting manufacturers into a trap which would effectively prevent them from selling ancillary and terminal equipment. The contention is rejected wholly as not based on any credible evidence.

Into the late 1970's Phonetele's management continued to write demanding letters to various BOCs demanding tariffing and to send copies to local regulatory agencies. In large part, tariffing was refused. Insofar as this sizeable correspondence is relied upon to show a "group boycott" the Court concludes that it does not show any such thing. The Court rejects the group boycott theory.

13. Intentional interference with advantageous business relationships: Plaintiff asserts the tort of intentional interference with advantageous business

relationships as a pendent claim. At argument, it became clear that the wrongful conduct which forms the basis of the alleged tort is the same alleged wrongful conduct which supports the antitrust claims. That being the case, the common-law tort claim is rejected. In addition to rejecting the allegations of wrongful conduct as the basis of the tort, the tort as an independent basis of relief has other problems (privileged conduct, lack of specific advantageous business relationships, etc.).

14. Conclusion. The Court concludes that plaintiff has failed to prove any of its antitrust theories. In those instances where the Court of Appeals has placed the burden of proof upon the defendants to justify the PCA requirement (the genesis of this lawsuit despite added issues), the defendants have presented

such evidence. The Court fully accepts the tests to be applied as specified in the Court of Appeals opinion--to wit, that there is no antitrust immunity for the defendants with regard to their protective connective arrangement tariffs filed post-Carterfone. However, alleged anti-competitive activity must be looked at under the rule of reason with a recognition of the regulatory context in which the Bell System operated. The Court concludes that the defendants have established by a preponderance of the evidence that, at the time the PCA requirements were in effect, the defendants had a reasonable basis to conclude that its action was necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority. Specifically, the defendants did reasonably conclude, given their expertise, that uncontrolled NCSU interconnection (and ancillary device

electrical interconnection) would endanger their own equipment or disrupt their own signal transmission in identifiable ways, thus justifying the PCA requirement while it was in effect. The Court also concludes that under the circumstances, the PCA requirement was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such real harm from occurring. Accordingly, judgment must be entered for the defendants.

Dated: July (14), 1988.

HARRY L. HUPP

HARRY L. HUPP
United States District Judge

FOOTNOTES

1 The following glossary of abbreviations is offered:

AT&T - American Telephone and Telegraph Company, the principal defendant and mother company in the Bell System, aka "Ma Bell" (since deceased);

BOC - Bell Operating Company, any of a number of subsidiaries of AT&T, providing telephone service in defined areas;

BSPPD - Bell System Purchased Products Division, a division of AT&T created about 1974;

Bell Labs - Bell Telephone Laboratories, Incorporated, a subsidiary of AT&T which does research, development, experiments, and design work for the Bell System;

Bell System - the aggregate total of the mother company and all of its subsidiaries, including the BOCs, Bell Labs, and Western Electric Company (the manufacturing subsidiary of AT&T);

CPUC - California Public Utilities Commission, the regulator of PT&T;

FCA - Federal Communications Act, the act passed by Congress in 1934 which causes federal regulation of, inter alia, the the interstate telephone system, and, thus, AT&T;

FCC - Federal Communication Commission, the commission created by the FCA to carry out the regulation of interstate communication

NARUC - a national association of state regulatory commissions;

NCSU - Network Control Signal Unit, a telephone device (such as a telephone or PBX) which imparts signals into telephone lines, routes calls to the intended

destination, and controls such functions as ringing, disconnection, billing, etc.;

PT&T - Pacific Telephone and Telegraph Company, the BOC covering California, the site of Phonetele's place of business and primary source of sales during its operating career;

PBX - Private Branch Exchange, a switching mechanism located on the premises of the telephone customer, through which calls to and from many extension telephones were funneled;

PCA - Protective Connecting Arrangement, a device containing transformers, capacitors, relays, etc., connected on the central office side of a customer provided piece of ancillary or terminal equipment electrically connected to the Bell System network, designed to regulate the amount or quality of voltage, signal strength, line imbalance, and signals entering the telephone wires;

CTD - a type of PCA;
ZZAGM - a type of PCA;
CTH - a type of PCA;
KTX - a type of PCA.

2 Phonetele, Inc. v. American Tel. & Tel. Co. (C.D.Cal. 1977) 435 F.Supp. 207.

3 47 USC § 151, et. seq.

4 Use of Recording Devices (1947) 11 FCC 1033.

5 Hush-A-Phone Corp. (1957) 22 FCC 112.

6 Carterfone (1968) 13 FCC2d 420.

7 Separation of the BOCs from AT&T was required by the Consent Decree in United States v. American Tel. & Tel. Co. (D.D.C. 1981) 524 F.Supp. 1336.

8 Carterfone (1968) 14 FCC2d 571 (on reconsideration) and AT&T "Foreign Attachments" Tariff Revisions (1968) 15 FCC2d 605.

9 Interstate and Foreign MTS and WATS, 56 FCC2d 593; (1976) 58 FCC2d 736.

10 Standard Oil Co. v. United States (1949) 337 U.S. 293, n.5; United States v. E.I. duPont De Nemours & Co. (1956) 351 U.S. 377.

11 (1968) 14 FCC2d 571.

12 AT&T "Foreign Attachment" Tariff Revisions (1968) 15 FCC2d 605, 609-10.

13 There has been some misreading of the record in the cases. In fact, it might be said that historical revisionism is not a monopoly of other cultures. At least two appellate cases, one in the Second Circuit and one in the Ninth Circuit, have stated that the Carterfone decision required the telephone company to permit connection of terminal equipment. From the quotations set forth in the text, it is clear that the Carterfone decision is limited to ancillary equipment. It is not even clear whether the ancillary equipment required to be attachable to the telephone system could be electrically connected or not--the Carterfone decision does not expressly say one way or the other. Nevertheless, two Court of Appeals decisions misread the word "interconnection" and the phrase "interconnected equipment" to refer to terminal equipment. Litton Systems, Inc. v. American Tel. & Tel. Co. (2d Cir. 1983) 700 F.2d 785, 794; International T. & T. Corp. v. General T&E Corp. (9th Cir. 1975) 518 F.2d 913, 933. The Court of Appeals in this case felt bound to adopt the International Tel. & Tel. interpretation (Phonetele, Inc. v.

American Tel. & Tel. Co., 664 F.2d 716, ftnt. 38.) Whether Carterfone required the attachment of terminal equipment, or the same was for the first time allowed by the post-Carterfone tariffs, is not significant for this decision, since the legal principle enunciated by the Court of Appeals opinion remains the same in either case. To the extent, however, that AT&T's motivation in filing the Carterfone tariffs is at stake, then the facts as they actually existed should be recognized. The fact is that Mr. Hy Romnes, then Chairman of AT&T, made the decision to allow the interconnection of terminal equipment through PCAs. He states that he did so to encourage the freest possible development of advances in telephone equipment. Plaintiff in this case sees the Carterfone tariffs as an anti-competitive ploy by the defendants. The facts are otherwise.

14 Ibid.

15 This holding was subsequently reiterated at least twice. See Interstate and Foreign MTS and WATS (1972) 35 FCC2d 539, 541-42; Telerent Leasing Corp. (1974) 45 FCC2d 204-206.

16 In Interstate and Foreign MTS and WATS (1972) 35 FCC2d 539, the FCC convened a "Joint Board" with the state agencies to study the effects of interconnection and a certification program. However, at that time, FCC declined to include a study of the economic consequences of interconnection. The state regulatory boards then started their own study through their national association.

17 Mebane Home Tel. Co. (1975) 53 FCC2d 473.

18 Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc. (1961) 365 U.S. 127.

19 United Mineworkers v. Pennington (1965) 381 U.S. 657. See also California Motor Transport Co. v. Trucking Unlimited (1972) 404 U.S. 508.

20 Interstate and Foreign MTS and WATS (1975) 53 FCC2d 221; Interstate and Foreign MTS and WATS (1975) 56 FCC2d 593, (1976) 58 FCC2d 738.

21 Litton Systems, Inc. v. American Tel. & Tel. Co. (2d Cir. 1983) 700 F.2d 785, cert. denied., (1984) 104 S.Ct. 984.

22 Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc. (1961) 365 U.S. 127.

23 United Mineworkers v. Pennington (1965) 381 U.S. 657. See also California Motor Transport Co. v. Trucking Unlimited (1972) 404 U.S. 508.

24 California Computer Products, Inc. v. IBM Corp. (9th Cir. 1979) 613 F.2d 727; Foremost Pro. Color, Inc. v. Eastman Kodak Co., (9th Cir. 1983) 703 F.2d 534.

APPENDIX C

No. 88-6353
IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PHONETELE, INC.,

Plaintiff-Appellant,

vs.

THE AMERICAN TELEPHONE AND TELEGRAPH COMPANY; WESTERN ELECTRIC COMPANY, INCORPORATED; BELL TELEPHONE LABORATORIES, INCORPORATED; PACIFIC TELEPHONE AND TELEGRAPH COMPANY,

Defendants-Appellees.

[No. CV 74-3566 HLH]

PETITION FOR REHEARING AND SUGGESTION FOR REHEARING EN BANC

ON APPEAL FROM
THE UNITED STATES COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
HON. HARRY L. HUPP, JUDGE

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Defendants-Appellees.

[No. CV 74-3566 HLH
Honorable
Harry L. Hupp]

PETITION FOR REHEARING
AND
SUGGESTION FOR REHEARING EN BANC

Introduction

Plaintiff-appellant Phonetele, Inc. ("Phonetele") petitions the Court for rehearing on the ground that the Court has erred on the following important points of fact or law:

1. The Court has misconstrued and/or ignored the controlling regulatory authority and there exists a conflict in the Circuits;

2. The Court failed to require that the district court apply the Law of the Case; and

3. The district court's 4 year delay in deciding the case is intolerable and seriously prejudiced Phonetele.

Phonetele respectfully suggests that all these points are appropriate for consideration by the Court en banc because such consideration is necessary to secure or maintain uniformity of its decisions, and the points involve questions of exceptional importance.

The Annotations

At oral argument on August 11, 1989, the Court suggested to ATT's counsel that perhaps post-argument "Annotations" to the record would be helpful to the Court. After argument, Phonetele expected the Court to order "Annotations". On August 23, 1989, Phonetele sent a letter

to the Court Clerk which stated that, unless Phonetele heard to the contrary, on or before September 15th, it would file "Annotations from the record tied to the trial court's Findings and Conclusions." Phonetele heard nothing to the contrary. Accordingly, on September 15, 1989, Phonetele sent 88 pages of Annotations to the Court.

Phonetele's Annotations were meticulously prepared, with detailed citation to the factual record (as suggested by the Court at oral argument). Apparently, the Annotations were only "received" and were neither filed nor considered by the Court in rendering its opinion. (see Section III, infra. for further reference to the Annotations).

Argument

I. THE COURT MISCONSTRUED THE CONTROLLING REGULATORY AUTHORITY AND THERE EXISTS A SPLIT IN THE CIRCUITS

At the heart of the case at bar lies ATT's tariff, FCC 263, which required a utility protective connecting arrangement ("PCA") as the exclusive means to connect non-utility terminal equipment ("CPE") to the telephone network. From the time of the earliest landmark case re terminal equipment, including Phonetele, "... the tariff is inescapably at the center of this controversy." Carter v. ATT, 365 F2d 486, 492 (5th Cir. 1966).

In Phonetele, Inc. v. AT&T, 664 F2d 716, 737-38 (9th Cir. 1981), known as Phonetele I, this Court prescribed a narrow affirmative regulatory defense ("Law of the Case"). At trial, AT&T failed to meet

any element of the prescribed defense. This Petition focuses upon mainly one element of the Law of the Case, that of regulatory justification. The Law of the Case required that ATT prove "... that its actions were necessitated by concrete factual imperatives recognized as legitimate by the regulatory authority ... ." ATT failed this test. Yet, on appeal, this Court condoned the trial court's fundamental error by asserting, "We conclude that regulatory justification as a defense to a monopolization claim similarly should be viewed as a factual inquiry ... ." (op. 13192). Thereby, this Court merely found that the district court's findings were not "clearly erroneous."

This Court also incorrectly cast Phonetele's position when it remarked that Phonetele merely challenged the factual support relied upon by the district court.

(op. 13184).[1] This Court erroneously excused the trial court's disregard of well established regulatory law which required the opposite conclusion, one in favor of Phonetele. Though the Law of the Case in Phonetele I mandated that ATT's conduct pass muster under regulatory law, by employing a wholly factual analysis, this Court redefined, and undermined, the Law of the Case.

In re Carterfone, 13 FCC2d 420 (1967) was the initial landmark case which

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[1]This is mistaken. From the onset, Phonetele has argued that prior regulatory disapproval of FCC 263 mandates a conclusion that the filing and implementation of the tariff in question necessitates a finding of monopolization. Therefore, this Petition, and even the entire appeal, could properly be decided merely by review of the regulatory law contained in a handful of cases. Phonetele also points out that under Evidence Code Rule 803(8)(c), the regulatory findings constitute part of the factual record. There is no way that ATT carried its affirmative burden in face of an imposing regulatory factual record (from 1967 forward) critical of the tariff.

opened up the telephone monopoly to CPE. Following Carterfone ensued years of extensive regulatory proceedings before both the FCC and the California PUC ("CPUC"). The regulators established well developed legal principles in the terminal equipment area. The resulting body of regulatory law requires a reversal of the district court. This is true because the unerring regulatory principle established that a PCA cannot be required based upon a mere potentiality of harm caused by CPE. PCAs are unreasonable, discriminatory, and unlawful as the exclusive means to connect CPE to the network.[2]

---

[2]Carter's antitrust case was originally remanded to the FCC under the doctrine of "primary jurisdiction". Carter v. ATT, 365 F2d 486 (5th Cir. 1966). An important purpose in remanding was to avoid a "... now-you-see-it, now-you don't sleight of hand ..." which "... would allow the tariff to be valid and yet invalid at one and the same time." (Carter at 495-96). This "sleight of hand" is precisely what a decision in ATT's favor accomplishes.

In November, 1975 and later in March, 1976, the FCC ruled that FCC 263 was "unreasonably restrictive" as well as "unlawful", and constituted "an unjust and unreasonable discrimination ... among suppliers of telephone equipment." (56 FCC2d 598-99) The FCC's express disapproval and finding of unlawfulness was grounded in the fact that FCC 263 specified PCAs as the exclusive means to connect CPE to the network. This Court ignored the FCC's specific regulatory findings and thereby condoned ATT's conduct which was proscribed under the strict showing required by the Law of the Case. This Court dismissed the FCC's rulings on the basis that the FCC merely decided that "registration was the best solution" and that the FCC's rulings against ATT occurred after ATT filed FCC 263. (op. 13193). This Court then improperly concluded that ATT had carried its affirmative

burden of proof. Such a conclusion is squarely contradicted by the regulators' disapproval of FCC 263. At best, over the years in question, the FCC took the position that ATT proceeded at its own risk. Other courts have been unimpressed with ATT's justification of its actions at issue here. Litton Systems, Inc. v. ATT, 700 F2d 785 (2nd Cir. 1983); United States v. ATT, 524 F.Supp 1336 (D.C. 1981).

The fact that the FCC did not declare FCC 263 unlawful until 1975, considered important to this Court, was of no real consequence to the issue whether ATT carried its heavy burden of proof at trial. The judgment in ATT's favor is unsupportable as a matter of law or fact based upon the regulatory findings and conclusions. Regulatory decisions explicitly recognize also that as to "ancillary" equipment, such as the PM, there is no issue -- certification

should have been enacted without delay after Carterfone. (see First Report and Order ("FRO"), 56 FCC2d 593 with Second Report and Order ("SRO"), 58 FCC2d 736.

The CPUC also expressly found that the charges for PCAs required by the tariff in question were "unnecessary and insisted upon by the utilities." Consequently, the CPUC ordered refunds of every PCA charge, ever collected on every type of CPE in California. (Decision No. 87920, 82 Cal. PUC 636 (1977), Decision No. 87620, 82 Cal. PUC 262 (1977)). While reciting this CPUC order in the blandest possible manner (op. 13191), this Court again accorded no significance to the CPUC's express regulatory disapproval of the tariff and its charges. The decision in ATT's favor cannot be squared with the regulatory test mandated by the Law of the Case.

Phonetele litigated against PTT and ATT for years before the CPUC. Phonetele's position was vindicated by the regulatory law which emerged. The resulting California Supreme Court decision, Phonetele v. PUC, 11 Cal.3d 125, 113 Cal.Rptr. 16 (1974), was unanimously decided in favor of Phonetele. Yet, this Court effectively sidestepped the CPUC litigation and Phonetele's Supreme Court victory. This Court seized upon the fact that the Supreme Court did not hold the PM could be directly connected or that certification was necessarily preferable to a PCA. (op. 13191) This court also noted that the Supreme Court did not vacate the CPUC's order that PCAs should remain in place. Neither of these observations about Phonetele v. PUC offers a scintilla of justification re ATT's conduct. Yet, this Court relied heavily on these points as if they somehow satisfied ATT's affirmative burden of proof. Suffice it to

say, in Phonetele v. PUC such matters of a wholly regulatory nature were not appropriate at that time for court ruling. The Supreme Court's treatment was entirely consistent with traditional deference accorded by courts to regulators in areas of regulatory expertise. The Supreme Court properly maintained the status quo re PCAs with full knowledge at the time that certification was imminent. The CPUC enacted a certification program about one year after Phonetele v. PUC.

The quintessential regulatory principle established in Carterfone, and its progeny through Phonetele v. PUC, holds that A PCA REQUIREMENT CANNOT BE JUSTIFIED ON THE BASIS OF POTENTIAL HARM TO THE TELEPHONE NETWORK. Based upon this simple principle, the Law of the Case requires that ATT make a showing of "real harm" as opposed to potential harm. The real harm must be identified prior to filing the tariff. (FRO,

at 596, "... this burden was to be met prior to filing of a tariff ... .") ATT failed to carry its burden of proof as a matter of law, since it demonstrated no "real harm" as to the PM or any other type of CPE prior to filing its tariff. By December, 1970, when Phonetele asked to connect, ATT had known for two years or more that it was unable to prove any harm caused by CPE. Nevertheless, it continued to advance false and exaggerated claims of harm from CPE. The FCC finally concluded that all terminal equipment, including ATT's, "... possesses the same potential for harm to the network. ... ." FRO, 56 FCC2d 593, 601 (1975). ATT knowingly told lies up to and including time of trial when it represented that CPE or the PM could harm the network. In the course of 8 years of regulatory hearings, ATT failed to prove any likelihood of harm from any CPE. The record contains numerous ATT admissions on this point.

Carterfone expressly invited ATT to file a tariff which publicly announces reasonable technical standards for interconnection; the FCC did not invite PCAs. ATT chose them. (Carterfone, at p. 424 "reasonable revised standards"). The tariff was ATT's own, dictated solely by ATT's business judgment. Proceeding at its own risk, and in the face of admonishment by the FCC, ATT filed a tariff providing for PCAs as the exclusive means to connect CPE. At the time of Carterfone, in 1967-68, numerous parties, including the FCC, made demands to ATT that it open up the network to broader interconnection. The FCC expressly admonished that the tariff was allowed to go effective without investigation or approval. (Carterfone, on reconsideration, 14 FCC2d 571, 574; ATT "Foreign Attachment" Tariff Revisions, 15 FCC2d 605, 610 (1968).

This Court accepted ATT's excuse that it was not in a position to "enact registration unilaterally". (op. 13189, f/n 9). This acceptance ignores the true facts because only ATT at the time knew the technical standards to connect to its telephone network. ATT could have readily filed the tariffs with standards for others to adhere to. Standards were even simpler for ATT than were tariffs for PCAs. This is true because the PCAs had to adhere to the identical standards. In the case of PCAs, ATT was required to maintain responsibility for development and furnishing of the PCA hardware. Incontrovertibly, a PCA approach maintained ATT's dominance ("bottleneck") since no one could connect unless ATT provided a piece of hardware called a PCA. This Court incorrectly assumed that registration, as it used the term, meant a "full-blown" registration. However, the FCC

expressly rejected "full-blown" registration of the type stubbornly insisted upon by ATT. (see FRO, particularly at pp. 598-601; SRO).[3]

In its most glaring error, this Court stated that "... both the CPUC and the FCC considered the PCA to be a reasonable, properly focused mechanism to prevent such harms from occurring." (op. 13193). This Court cited no authority in support of this single pivotal point; none exists. As a matter of law, the regulatory cases reveal that exactly the opposite is true.

[3] In PHONETELE I, this Court stated that, "The defendants may not justify their actions based on some mistake of law in interpreting the FCA, or judicial or FCC decisions." 664 F2d at 738. Cut to essentials, this is precisely the main weakness in ATT's defense and why it fails. ATT, and apparently the Court, assumed that "registration" meant a full-blown program dealing with installation, repair and maintenance. The FCC expressly rejected any notion of full-blown registration as ATT's attempt to postpone the inevitable, e.g. registration of a simple type. Only reluctantly did the FCC enact simplified registration after 8 years of intransigence by ATT. (See FRO and SRO, supra.)

Both the CPUC and the FCC found the PCA to be unreasonable, unlawful and discriminatory against users and manufacturers of CPE. THIS ONE CHANGE IN FINDINGS, REQUIRED BY THE REGULATORY DECISIONS, WOULD NECESSITATE REVERSAL OF THE DISTRICT COURT. For this reason alone, rehearing is appropriate and the decision issued November 6, 1989, should be withdrawn.

Litton Systems, Inc. v. ATT, supra. involved a terminal equipment case by Litton against ATT. The essential facts in Litton are virtually identical to the facts in Phonetele's case; Phonetele's are more favorable in that the PM is ancillary equipment. The respective regulatory backgrounds are identical. All of the important evidence in the Litton record is in evidence in the instant case. There exists a conflict on a point of law in the Circuits because this Court misconstrued the

regulatory law; Litton properly applied it in finding against ATT. (see particularly at pp. 806-812). Litton found, "Opposition to certification is simply the other side of the interface tariff coin; AT&T's filing and maintenance of the PCA requirement was the very embodiment of opposition to the only feasible alternative -- certification standards. ... AT&T made unsupportable claims to the FCC regarding network harm, ... and generally attempted to buy as much time as possible to improve its own competitive position at the expense of Litton and other competitors." (at p. 809).

II. THIS COURT FAILED TO REQUIRE THE DISTRICT COURT TO APPLY THE LAW OF THE CASE

On pages 13185-86 of its opinion, this Court quoted the Law of the Case from Phonetele I. The district court acknowledged

the Law of the Case constituted its "marching orders". The essential elements are: If ATT can establish that, at the time of the events: (1) it had a reasonable basis to conclude that its actions were "necessitated" (2) "by concrete factual imperatives" (3) "recognized as legitimate by the regulatory authority", then its actions would not violate the antitrust laws. In Phonetele I, this Court explained further that the inquiry would depend upon whether the facts show that the companies "did reasonably conclude, given their expertise" that uncontrolled interconnection would "endanger their own equipment or disrupt their own signal transmissions in identifiable ways, and also that the tariff as filed was a reasonable, properly focused mechanism, considering other alternatives then available, to prevent such real harm from occurring." (op. 13185-86). The district

court never applied these tests. This Court has failed to require that the district court follow its marching orders.

No real harm was ever identified which would endanger ATT equipment or personnel. As to the Phonemaster ("PM") manufactured by Phonetele, this is particularly true, because the CPUC decision against Phonetele (which had found only "potential" harms) was annulled in Phonetele v. PUC for the reason that potential harm is insufficient to justify a PCA. In one of the rare instances where the trial court ruled correctly, it found that the PM was not harmful to the network. Also, it stands undisputed in the record that beginning with PTT in 1974, several ATT companies actually supplied the PM under tariff as utility-provided equipment. Prior to tariffing, no major modifications of the PM were required.

It is inescapable that the tariff mechanism itself is antithetically opposed to a "reasonable, properly focused mechanism." This is readily observed because the undisputed evidence demonstrates that FCC 263 merely requires a "connecting arrangement" (non-protective). Before a PCA could be used for hook-up, in each of the 50 state jurisdictions, the 23 ATT Operating Companies would have to price and file separate local tariffs on each PCA. (Because PCAs were "intrastate" equipment). Therefore, Phonetele, as well as any other companies relying upon PCAs, were forced to address a multitude of PCAs and to duplicate the process in state after state. No tariffs were ever filed to connect the PM outside of California.

Phonetele I held there was no implied immunity as a consequence of regulatory supervision. In the instant appeal,

the Court effectively grant ATT an immunity based upon even a lesser showing of necessity" for its actions than this Court has already rejected. Since Phonetele I, the parties have been involved in litigation over eight years. By affirming a judgment for ATT, this Court renders nugatory Phonetele I, even in the face of a complete absence of reasons to grant ATT an immunity now. Such a result is unconscionable, unjust, and a needless waste of the litigants' and the courts' time and resources.

III. THE FOUR YEAR DELAY SERIOUSLY UNDERMINED A FAIR DECISION IN THE CASE

This Court has now established an intolerable rule that an "appalling" delay of four years, by itself, absent prejudice, is excusable. In the instant case, the delay gravely prejudiced Phonetele.

Indeed, this Court suggests that remand or reversal might be appropriate if there existed either (1) "strong independent support" that the district court departed from its proper role or (2) if there were "a convincing showing of prejudice." (p. 13198-99). Both showings were evident on the record.

Point 1 -- On July 30, 1987, 3 years after submission of the case to the district court for decision, Phonetele filed a Petition for Writ of Mandamus requesting that this Court order a decision. Case No. 87-7326 resulted and Phonetele requests that the Court take judicial notice of the contents contained in Case No. 87-7326. On June 6, 1988, after the Petition had languished almost one year and the district court missed two deadlines, the district court issued a proposed Opinion. The strong inference is that the district

court did not follow its proper role to render an opinion while matters were fresh in the Judge's mind. The temptation of the court was irresistible to place undue reliance upon ATT's written testimony four years after submission of a complicated matter.

Point 2 -- ATT itself notified the court of almost 80 errors within its proposed Opinion. The final Opinion of July 14, 1988, was little changed from the proposed one. The district court's final Opinion is rife with fundamental factual errors. Phonetele's Annotations, apparently not considered by this Court, painstakingly addresses these errors. The Annotations well support that Phonetele was prejudiced by a district court which frantically attempted to render an opinion although its grasp of the record was tenuous at best. Proof of the pervasive factual errors contained within the district court's Opinion provides "strong independent support" of prejudice to Phonetele

from the delay. Only by reading Phonetele's Annotations, can this be convincingly demonstrated. This Court's failure to consider the Annotations pre-ordains the incorrect result that Phonetele failed to make a "convincing showing of prejudice."

Conclusion

Next month, this action is fifteen years old. "Justice delayed is justice denied." A four year standard of delay for the federal judiciary which this Court has condoned is unacceptable; it is not justice. Even worse than unexcused delay, however, is the fact that the decision has been decided against Phonetele even though no good reason in law or fact exists for such a result. Under the Law of the Case, a heavy burden was imposed upon ATT which it did not meet. In Phonetele I, this Court decided ATT enjoyed no immunity. In the instant appeal, the Court has in effect granted immunity

because ATT has utterly failed to prove any regulatory justification. None exists.

Phonetele is left with the unmistakable impression that the result in this case has little to do with the evidence or law. If the result were guided by these principles, ATT could not be the prevailing party. Basically, it appears that the case is so old, that the court has wearied of it.[4] In proof of this, as demonstrated

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[4]In fact, the Court stated as much: "To vacate and remand a decision which the district court has spent several years crafting hardly seems a sensible means to reduce delay." (op. 13198). If the district court decision is incorrectly decided, any incidental "delay" occasioned by redressing the wrong would be fully justified. Phonetele's case has neither been justly decided nor well considered. The reference to the "crafting" by the district court is wholly unwarranted. For the first three years or more after trial, the trial court did nothing. By then, the record lay ice cold. Any delay attendant to reversal is contemplated by the administration of a system of justice. The delay attendant to a reversal and remand would be laudatory if this Court would redress the dire consequences resulting from the district court's unconscionable negligence.

above, the pivotal point in this Court's decision stands entirely unsupported by any authority. The regulatory authority in fact compels the opposite result. The well developed findings of fact and law which the regulators have established in exercise of primary jurisdiction stands firmly against ATT. Phonetele I accorded ATT a narrow affirmative defense. ATT's position on almost every point has been repeatedly rejected by the regulatory authorities. Yet, ATT wins the antitrust case. This constitutes an impossible result, a "sleight of hand" referred to in footnote 2, above.

For the foregoing reasons, Phonetele respectfully requests that this Court grant rehearing and suggests that the Court conduct such rehearing en banc. Specifically, Phonetele requests reversal and remand to another court for retrial on

any unresolved liability issue(s). The bifurcated case should then proceed to trial the issue of damages.[5]

DATED: November 17, 1989

Respectfully submitted,

/s/
RICK M. STEIN
Sanger & Stein

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[5]The Court's Opinion contains suggestion that Phonetele was not damaged by the PCA requirement in California because the charges were stayed or Phonetele could have avoided duplicative circuitry in the PM. Under analysis, extensively briefed in the Annotations, clearly these points are "make-weight" as to the fact of damage. Also, ATT refused to make available, or file tariffs for, any PCA for Phonetele's use outside of California, thereby barring Phonetele from the marketplace. There really can be no serious question as to the fact that Phonetele was damaged as a result of ATT's misconduct. The PM was years ahead of its time and was a proven, quality product with market demand. The bifurcated case has not been before the trial court on the question of damages.

No. 88-6353

(CERTIFICATE OF SERVICE BY MAIL - RULE 25, F.R.A.P.)

YVONNE A. GREVE certifies that she is a citizen of the United States, over 18 years of age, a resident of the County of Los Angeles, and not a party to the within action; that her business address is 732 East Washington Boulevard, Los Angeles, CA 90021; that on the 17th day of November, 1989, she served the within Petition for Rehearing & Suggestion For Rehearing En Banc on the following named parties in said action, by placing two true copies thereof in an envelope addressed to the attorney(s) of record for said parties as follows:

Kenneth K. Howell, Esq.
Sidley & Austin
Attorneys at Law
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Los Angeles, CA 90067

and by then sealing said envelope and depositing the same, with postage thereon fully prepaid in the United States mail at Los Angeles, California; that there is a delivery service by United States mail at the place so addressed, or there is a regular communication by United States mail between the place of mailing and the place so addressed.

I certify under penalty of perjury that the foregoing is true and correct.

Dated at
Los Angeles, California

November 17, 1989

/s/ (YVONNE A. GREVE)

C-196

APPENDIX D

FILED

OCT 17 1991

CATHY A. CATTERSON, CLERK
U. S. COURT OF APPEALS

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

PHONETELE, INC., Plaintiff-Appellant, vs. AMERICAN TELEPHONE & TELEGRAPH COMPANY, et al., Defendants-Appellees.	No. 88-6353 D.C. #CV-74-3566-HLH ORDER

Before: FLETCHER, and NELSON, Circuit Judges, PHILIP M. PRO,* District Judge.

The panel as constituted in the above case has voted to deny the petition for rehearing.

The full court has been advised of the suggestion for rehearing en banc and no judge of the court has requested a vote on it.

Fed. R. App. P. 35(b).

The petition for rehearing is denied and the suggestion for rehearing en banc is rejected.

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* Hon. Philip M. Pro, United States District Judge for the District of Nevada, sitting by designation.